Cit Vs. M/S V.R.V. Breweries and Bottling Industries Ltd.

Cit Vs. M/S V.R.V. Breweries and Bottling Industries Ltd.

SooperKanoon Citation : sooperkanoon.com/920647

Court : Delhi

Decided On : Aug-19-2011

Judge : Sanjay Kishan Kaul; Rajiv Shakdher, Jj.

Acts : Income Tax Act, 1961 - Sections 37, 35A, 40A(2)

Appeal No. : ITA Nos. 594/2005, 646/2005 & 559/2006

Appellant : Cit

Respondent : M/S V.R.V. Breweries and Bottling Industries Ltd.

Advocate for Def. : Mr Ajay Vohra; Ms Kavita Jha; Mr Somnath Shukla, Advs.

Advocate for Pet/Ap. : Ms Rashmi Chopra, Adv.

Judgement :

1. The Income Tax Appellate Tribunal (in short the Tribunal) by a common judgment dated 29.07.2004 has disposed of cross appeals of the assessee and revenue for assessment years 1997-1998, 1998- 1999 and 1999-2000. The said judgment of Tribunal has given rise to the three (3) captioned appeals. It is important to note that while for each of the assessment years under consideration (i.e., assessment year 1997-1998, 1998-1999 and 1999-2000) the Assessing Officer has passed orders (on the issue with which we are concerned in the captioned appeals) against the assessee, the Commissioner of Income Tax (Appeals) [hereinafter referred to as „CIT(A)] has taken a view in favour of the

assessee in the assessment year 1998-99. Since the facts obtaining in the captioned appeals are common and the Tribunal has dealt with the cross appeals by a common judgment, we intend to dispose of the captioned appeals by a common judgment.

2. The assessee at the relevant time was in the business of manufacturing and sale of Indian Made Foreign Liquor (in short „IMFL) at the Pathankot, Punjab when, evidently, it entered into an agreement dated 06.07.1996 (in short the „said agreement) with a public limited company by the name of Shaw Wallace Co. Ltd. (in short „SWCL) for the purposes of manufacturing IMFL products under the brands owned by SWCL or its associated or related companies. The said agreement comprised of following addendums:

(i) Annexure 1 provided for: General Terms and Conditions which were to operate inter-se the parties.

(ii) appendix „A provided for: specification of spirit.

(iii) appendix „B provided for: specification of demineralized water to be used for reducing the strength of spirit.

(iv) Appendix „C provided for: trademarks/ brand names etc.

(v) Appendix „D provided for: consideration to be paid by the assessee.

(vi) Appendix „E provided for: Packing material wastage standard.

3. In so far as the General Terms and Conditions contained in annexure „1 to the said agreement are concerned, the following clauses would perhaps be relevant to draw out the broad obligations undertaken by the assessee. We propose to extract the same to the extent they are relevant:

"2. ARRANGING FOR SPIRIT AND UTILISATION THEREOF 2.1 Shaw Wallace will supply to the UNIT sample of spirit normally used by Shaw Wallace in the manufacture of IMFL products. The sample spirit shall be in accordance with the specifications and tolerances given in Appendix „A. 2.2 The UNIT shall procure spirit in such form as may be agreed to by Shaw Wallace in conformity with the

sample, specifications and tolerances in such quantities as may be required for the purpose of utilizing the same for the manufacture of IMFL products.

2.3 Unless otherwise agreed in writing the „spirit shall mean manufactured and distilled out of raw materials molasses.

2.4 xxxx

2.5 xxxx

2.7 xxxx

3. MANUFACTURE/BOTTLING OF IMFL

3.1 The UNIT hereby undertakes to manufacture different brands of IMFL, which Shaw Wallace may specify taking into account the market condition from time to time. 3.2 xxxx

3.3 Unless otherwise agreed to in writing the IMFL products shall be supplied and delivered to the purchasers in bottles sealed, labeled and packed in cartons. 3.4 xxxx

3.5 xxxx

3.6 The packing material shall be as per the specifications of Shaw Wallace as regards size, shape, design, quality etc. Such packing materials shall also conform to the statutory regulations as may be laid down from time to time by the Excise and other authorities. The packing materials shall prominently display the trade/brand names of Shaw Wallace and such other brand/trade names as Shaw Wallace may designate from time to time.

3.7 The UNIT shall purchase the packing materials after getting the samples approved by Shaw Wallace and on terms to be approved by Shaw Wallace.

3.8 xxxx

3.9 xxxx

3.10 If any IMFL product is declared unsaleable in any state on account of its being under strength the UNIT undertakes to take back all such mocks and reprocess them so as to conform to the required specification. All expenses incurred in this connection will be to the account of the UNIT.

If stocks are required to be taken back for other reasons, such as, sedimentation etc. the UNIT shall obtain necessary permission from the Excise Authorities for taking back such stocks and arrange for re-processing, the parties will then examine the causes of such defect and the party to bear the cost for the same will be mutually agreed upon based on the report of such examination. The intention of providing for the above terms is to ensure that only quality products are sold in the market under the brand names belonging to or designated by Shaw Wallace

4. EXCISE FORMALITIES

4.1 xxxx

4.2 All excise formalities required fo the UNIT (Distillery) shall be the responsibility of the UNIT. The above shall include the registration of the labels with the Excise authorities, obtain permission from the Excise Authorities for the manufacture, bottling, blending, storage, selling and supplying of IMFL products of brands mentioned above and for the use of packing materials as per specifications and requirements of Shaw Wallace as well as for use of Shaw Wallace labels.

4.3 The obtaining of Export passes as may be necessary for the purpose of despatches of the IMFL products manufactured bottled supplied by the UNIT under this agreement shall be the responsibility of and to the account of the UNIT. The responsibility for arranging the import permits as may be necessary for arranging such despatches shall not however be the responsibility of the UNIT.

4.4 The import permits as may be necessary for the purpose of sale and supply of the IMFL products etc. manufactured from the UNIT to the purchaser shall be arranged by Shaw Wallace or the persons designated by Shaw Wallace for purchase of IMFL products. The import permits shall be sent to the UNIT along with the indents with full particulars of the type of products to be dispatched by the

UNIT and the place, date and mode of such dispatch.

4.5 xxxx

5. xxxx

6. TRADE MARKS AND MARKETING

6.1 The trade marks, brand names, design and the get up in which the IMFL products will be sold, supplied and delivered by the UNIT and in particular and not limited to those listed in APPENDIX „C hereto shall always be the sole property of Shaw Wallace or its associate or related companies as the case may be.

6.2 The UNIT hereby acknowledges and accepts that the UNIT never had nor has any right, title or interest therein and shall not at any time claim any right whatsoever to the use of the labels, brand names, trade marks and or get up of the IMFL products belonging to Shaw Wallace or to the nominees associates of Shaw Wallace except under written permission from Shaw Wallace.

6.3 Shaw Wallace hereby authorizes the UNIT as a licensee, under a separate agreement to manufacture, process package and sell the IMFL products of various brands of Shaw Wallace as contained in the APPENDIX „C and such other brands as may be agreed upon from time to time for which Shaw Wallace or its associate or related or nominee company own or will own valid trademark registrations in India or otherwise which names, brands, etc. belong to or are associated with Shaw Wallace or any such other companies mentioned above.

6.4 Shaw Wallace from time to time advise the UNIT as to the marketing arrangement for IMFL of brand names belonging to Shaw Wallace or brands designated by the Shaw Wallace and the UNIT shall act in accordance with the directions of Shaw Wallace in so far as the sale of above brands of IMFL.

6.5 Nothing herein contained or implied shall be construed as precluding in any manner Shaw Wallace or its associated companies or related companies as the case may be from using or licencing the use of the said trademarks or brand names or get up on any goods including IMFL in India of elsewhere.

6.6 xxxx

7. CONSIDERATION

7.1 Royalty including charges for services to be rendered by Shaw Wallace are payable by the UNIT to Shaw Wallace at the rates and in the manner set out in APPENDIX „D hereto. The parties may mutually agree to revise the above changes from time to time.

7.2 The UNIT shall be liable to pay the royalty due to Shaw Wallace as specified in the agreement entered into between the parties within the time specified in APPENDIX „D.

7.3 No such royalty etc. shall be payable in respect of the IMFL products which are purchased by and supplied to Shaw Wallace under import permits obtained in the name of Shaw Wallace. In the case of such purchases Shaw Wallace shall pay the price of IMFL at the rate mentioned in APPENDIX „D. In the case o sale to Permit Holders other than Shaw Wallace the UNIT shall include in the price marketing, royalty and service charges as may be advised to the person undertaking the marketing of the IMFL products.

7.4 xxxx

7.5 xxxx

8. DURATION, TERMINATION AND CONSEQUENCES TEHREOF

8.1 xxxx

8.2 xxxx

(a) Upon completion of the period of 5 years unless terminated earlier or renewed ____ the said period of five years, or

(b) xxxx

8.3 Upon such determination of this agreement the UNIT shall cease to be a licensee or registered user of the trade marks or brand names of Shaw Wallace

and shall not have any right to use such trademarks or brand names thereafter. The UNIT agrees to cease and desist forthwith from using the said trade marks, brand names, get up of Shaw Wallace and or any similar trademarks upon termination of this agreement for any reasons whatsoever in respect of the goods of Shaw Wallace or goods of the same description or any other goods.

8.4 xxxx

9. xxxx

10. xxxx

11. ASSIGMENT

The UNIT shall not assign subject or part with the rights and obligations under this Agreement which are personal to the UNIT provided however Shaw Wallace may at any time designate any of its subsidiary company to undertake the work under this Agreement and be the beneficiary of the terms and conditions of this agreement.

4. At this stage it may also be relevant to note that in so far as the provision for consideration payable under the said agreement is concerned, the details are largely provided in appendix „D. The relevant portion of appendix „D reads as follows:

"CONSIDERATION

1. The prices at which Shaw Wallace will purchase IMFL products from the UNIT will be computed as under:

i) Actual cost of Sprit incurred by the UNIT as per Shaw Wallaces direction Plus

ii) Actual cost of Electricity and Water charges Plus

iii) Actual cost of Labour and other expenses which are incurred by the UNIT (with the prior approval of Shaw Wallace) Plus

iv) Actual Excise Establishment expenses Plus

v) Bottling charges at the rate of Rs 15/- per case (to be reviewed by Shaw Wallace on an annual basis) Plus

vi) Packing Materials on actual basis plus wastage as per Annexure „E specifying individual items of packing materials with standard allowable wastages Plus

vii) Cost of chemicals for conversion at the rate of Rs 0.50 per case (to be reviewed by Shaw Wallace on an annual basis)."

2. Shaw Wallace will be responsible to sell and arrange for collection of sale proceeds and declaration forms required for sales tax to / from Direct Indentors. The payment shall be made by Direct Indentors by way of Cheque or DD in the name of the Unit. The UNIT, after deducting the value of each product at applicable rates as specified above and the amount representing the statutory dues like Sales Tax, Excise Duty etc., will pay the balance amount to Shaw Wallace (which represents Royalty/ Marketing services charges etc.)

(emphasis is ours)

5. Based on transaction which have emanated from the said agreement, the authorities below have returned the following findings for each of the assessment year. We shall briefly refer to the findings of each of the authorities in respect of the assessment years in issue.

ASSESSMENT YEAR 1997-98

6. The Assessing Officer noted that the assessee had debited an amount of ` 84,01,160/- as payments towards royalty. The assessee had rendered its justification, as noted by the Assessing Officer, vide two letters dated 24.01.2000 and 10.03.2000. By the said letter the assessee had briefly made reference to the said agreement adverted to hereinabove by us. The assessee had indicated evidently that it had executed the said agreement due to lack of demand for its products which was, prior to the agreement, sold under the assessees own brands. The assessee justified the payment on the ground that the arrangement had proved successful and beneficial for its business in as much as it had produced 61634 cases of IMFL as against 621 cases in the earlier year. The

assessee went on to suggest that under the said agreement, SWCL provided brand names, sample of spirits, labels, arranged supply of raw- materials and sale through a chain of its customer, which proved beneficial to the assessee. Consequently, the assessee debited in its accounts the amount of royalty paid to SWCLin consonance with the said agreement. The assessee submitted that the amount paid was expended wholly and exclusively for its own business and hence, the expenditure incurred deserved to be allowed fully.

7. The Assessing Officer, however, disagreed with the explanation rendered by the assessee as according to him, this was a case of „transfer of income having been undertaken by employing a device of setting up a separate entity. The Assessing Officer came to the conclusion that the day-to-day management and control of the assessee company lay with the Shaw Wallace Group. The fact that the Shaw Wallace Group held majority shares in the assessee was not even disclosed in the audit report or, notes to the accounts or even in the tax audit report, and that, this fact emerged only during the course of assessment. The Assessing Officer compared the bottling charges, which were received by another entity by the name of Balbir Distilleries Limited located at Solan, Himachal Pradesh from SWCL, with that, which were received by the assessee. According to the findings returned by the Assessing Officer, Balbir Distilleries Ltd. received towards bottling charges ` 40 per case in 1995, while the assessee received only ` 15 per case, pursuant to the said agreement, which was decidedly executed between the assessee and the SWCL a year later, i.e., in 1996. According to the Assessing Officer this was a case of transfer of profits.

7.1 Furthermore, the Assessing Officer, on perusal of the terms of the agreement, came to the conclusion that the assessee had acquired right to manufacture and, sale of IMFL products under the SWCL brand name. The Assessing Officer was thus of the view that the payment made by the assessee towards use of trademarks, brand names, designs and get up were in the nature of capital expenditure, and that SWCL had authorized the assessee in that regard vide a separate agreement, which despite repeated directions had not been produced by the assessee. Reference in this regard was made to Clause 6.3 read with appendix „C annexed to the said agreement.

7.2 For the aforesaid reasons, the Assessing Officer rejected the alternative claim of the assessee to allow deduction under Section 37 of the Income Tax Act, 1961 (in short „I.T. Act). Furthermore, having held that it was in the nature of capital expenditure and hence not an expenditure allowable under Section 37 of the I.T. Act, the Assessing Officer concluded that the assessee had acquired patent rights for the use in its business, and therefore, the condition stipulated under Section 35A of the I.T. Act was satisfied.

7.3 The Assessing Officer went on to observe that a part of the royalty paid was excessive in nature. He proceeded, however, to restrict the expenditure to 1/14th of the amount claimed in the year in issue by invoking provision of Section 35A. Consequently, a sum of ` 78,01,077/-, being 1/14th of the claimed amount, i.e., ` 84,01,160/- was disallowed.

8. Aggrieved by the same an appeal was preferred by the assessee in respect of this aspect with the CIT(A). The CIT(A) proceeded to examine the issue with reference to the application of provisions of Section 40A(2) and Section 35A of the I.T. Act. In so far as the provisions of Section 40A(2) are concerned the CIT(A) adverted to the following:

"The appellants case is covered under clause (iv) of subsection (b) where a company having a substantial interest in the business or profession of the assessee is covered for this purpose. The substantial interest is also defined in the Explanation thereto. According to this if a company has 20% of the voting power or more it is said to have a substantial interest. The AO has already pointed out that the majority share holding is by the SW which has not been contravened. The Ld AR further submitted that the employees of SW have the controlling share holding. Therefore, the payment of royalty to SW is covered under section 40A(2) and it has to be seen whether the payment is excessive or unreasonable."

8.1 In conjunction with the above, the CIT(A) took note of the difference in bottling charges paid to Balbir Distilleries Ltd. as against that which was paid to the assessee. The CIT(A) sustained the findings of the Assessing Officer that this was a case of transfer pricing. Accordingly, he disallowed a sum of ` 24,70,929/- out of the total sum claimed, i.e., ` 84,01,160/- under Section 40A(2) of the I.T. Act. As

regards the balance sum, i.e., ` 59,30,231/- (84,01,160 - 24,70,929) he applied the provisions of Section 35A of the I.T. Act.

Thus in consonance with the provisions of Section 35A, the CIT(A) allowed 1/14th of the said amount, i.e., ` 4,23,588/-. Resultantly, the CIT(A) in fact disallowed an amount equivalent to ` 79,77,572 (24,70,929 + 55,06,643). As against this, the Assessing Officer had disallowed an amount of ` 78,01,077/-.

ASSESSMENT YEAR 1998-1999

9. In this assessment year, the Assessing Officer noticed that the assessee had claimed a sum of Rs.5,67,92,000/- as royalty paid to SWCL since in the immediately preceding year (i.e., A.Y. 1997-1998), the Assessing Officer had allowed only 1/14th amount towards royalty to the assessee by invoking the provisions of section 35A of the IT Act. He adopted the same methodology. Consequently, apart from a sum of Rs.4,05,671/- which was 1/14th of the amount claimed, the balance sum amounting to Rs.5,27,35,429/- was disallowed.

9.1 Being aggrieved, the assessee carried the matter in appeal to the CIT (A). The CIT (A) considered the matter from two angles. The first being: whether the payment made by the assessee for use of trademark and services rendered by SWCL was in the nature of capital or revenue expenditure? If the inquiry resulted in coming to the conclusion that the payment was in the nature of capital expenditure, whether it was covered under the provisions of Section 35 A of the IT Act.

9.2 Besides this, the CIT(A) also examined the matter as to whether the payments made to SWCL were unreasonable and hence, hit by the provisions of section 40A(2) of the IT Act.

10. In so far as the first aspect was concerned, the CIT (A) on applying the ratio of the decision of the Supreme Court in CIT v. Ciba of India Limited (1968) 69 ITR 692 SC came to the conclusion, after interpreting various clauses of the agreement, which interalia included, the termination clause, and clause 9 which, required the assessee to maintain strict confidence in respect of communication,

correspondence, records and information, knowledge and documents falling within its domain - that at no stage did SWCL part with any asset of its business. According to the CIT (A), the assessee did not acquire any asset of enduring nature; the expenditure incurred by way of royalty was for the purposes of business and hence, in the nature of revenue expenditure. A particular reference was made to the fact that expenditure was incurred by the assessee not only for use of trademark but also towards services rendered by SWCL, in connection with, quality control of "sample of spirit" provided to it, purchase of raw materials, packing materials and in obtaining import permits, etc.

11. In so far as the second aspect is concerned, i.e., whether the payments were hit under section 40A(2) of the IT Act, the CIT (A) returned the following finding of fact while disagreeing with the view taken by the CIT(A)-XIV, New Delhi vide his order dated 20.02.2001 pertaining to Assessment Year 1997-1998 :-

"The second issue relates to the applicability of provisions of Sec. 40A(2). The equity capital of the appellant company as on 31.3.1997 was held by the following investment companies and individuals and number of shares held by them are indicated against their names:

i) Alaknanda Manufacturing and 5,18,800 Finance Ltd.

ii) Tribtis Investment Ltd. 4,50,000 iii) Manaswar Wall Investment Ltd. 3,60,000 iv) Canver Investment Ltd. 1,35,000 v) Maharashtra Distilliaries Ltd. 87,930 vi) Sh. Suraj P. Gupta 8,61,610 vii) Six individuals holding shares 10 60 each

It may be noted that not a single share is not held by the Shaw Wallace & Co. Ltd....."

5.3 .....

In the instant case the payment has not been made to any director of the company or any relative of a director, partner or member who has substantial interest in the company. Shaw Wallace & Co. is not holding any equity shares in the company. Now the question arises whether the payment made to Shaw Wallace which has distant and indirect control on the assessee can be said to be a person having

substantial interest in the appellant company. The expression "substantial interest" has been defined in Explanation 2 to sub-section (2) of Section 40A. A person is deemed to have substantial interest in the business or profession of such person is beneficial owner of at least 20% of equity capital in case of a company. The expression "not less than 20% of voting power" implies that the person must hold equity shares directly and not distantly. Therefore, Shaw Wallace & Co Ltd. cannot be said to be the beneficial owner of shares of the appellant company.....

.....From the list of share holders it is clear that the employees of Shaw Wallace do not have the controlling share holding. Six individuals are holding ten shares each and Sh. Suraj P. Gupta held 8,61,610 shares. Shri Suraj Gupta is not employee of the appellant. Further the payment has not been made to Shri Suraj P. Gupta or his relative of the company of which he is a director. I would like to mention here that the CIT (A), SIV, New Delhi had made reference to finding of the Assessing Officer that the majority share holding is by the Shaw Wallace which has not been controverted. However, the appellant for the Asstt. Year 1998-1999 has controverted this fact. The shares are neither held by the Shaw Wallace nor by the employees of Shaw Wallace as also the payment of royalty was not made to the employees of Shaw Wallace. Further payment was not made to Sh. Suraj P. Gupta who was holding more than 20% shares. Therefore, the provisions of Section 40A(2) will not be applicable to the facts of the instance case. The Assessing Officer has not brought any material on record to justify his conclusion as to how the provisions of section 40A(2) will be applicable.....(emphasis is ours)

5.4.....In the instant case, the payment has not been made to the specified persons under section 40A(2)(b) and therefore, provisions of section 40A(2) are not applicable. Since provisions of section 40A(2)(b) are not applicable, the question for estimating excessive amount of expenditure does not arise though the appellant has given explanation for differential rate of payment of bottling charges to the Balbir Industries...." (emphasis is ours)

ASSESSMENT YEAR 1999-2000

12. The Assessing Officer noticed a sum of Rs.10,20,35,544/- had been debited to the profit and loss account as payments made on account of royalty to SWCL. The

Assessing Officer more or less adopted the view taken in the Assessment Year 1997-1998 and came to the conclusion that the assessee had alongwith SWCL put in place the present arrangement only to transfer profits. The Assessing Officer in the net result allowed only 1/14th of the amount claimed; resultantly, a sum of Rs.9,97,78,120/- was disallowed.

12.1 Being aggrieved, the matter was carried in appeal by the assesse once again to the CIT (A). The CIT (A) in this assessment year agreed with the views taken by his predecessor in the Assessment Year 1997-1998, while disagreeing with the view taken by his other predecessor in the Assessment Year 1998-1999. The net result was that CIT (A) confirmed the disallowance of Rs.9,97,78,120/- as ordered by the Assessing Officer.

13. As noticed in the very first paragraph hereinabove, appeals were filed both by the revenue and the assessee. The assessee was in appeal before the Tribunal in respect of orders of the CIT (A) for the Assessment Year 1997-1998 and 1999-2000, while the revenue was in appeal in respect of the order of the CIT (A) for the Assessment Year 1998-1999. The Tribunal vide impugned judgment has decided the issue by way of a common judgment. The Tribunal in the impugned judgment, upon perusal of the terms of the said agreement has returned the following findings of facts: (i) under the agreement the assessee had acquired a right to manufacture and, sale of brands of SWCL; (ii) out of the gross royalty payable to SWCL rebate and discount was required to be allowed. SWCL was thus entitled to receive only the net amount of royalty after the adjustment of rebate and discounts to the customers; (iii) Under the said agreement SWCL was required to supply to the assessee only sample of spirits; (iv) SWCL was obliged to specify the raw materials required for manufacture, distillation and bottling of products and render advice on the purchase of packing material to enable the assessee to retain quality control; (v) SWCL was also required to render its service for acquiring import permits and obtaining certificates from the excise authorities, besides giving advice to the assessee qua marketing arrangements being adopted in respect of sale of IMFL products; (vi) and finally, apart from the pregoing SWCL was also required to render financial support to the assessee.

14. Based on the aforesaid findings, the Tribunal came to the conclusion that the royalty was paid by the assessee to SWCL for carrying out day-to-day business activities. The payment made under the agreement enhanced, promoted the assessees product and added to its business efficiency. The Tribunal concluded that the sale turnover as well as the profitability of the assessee had increased pursuant to the operability of the said agreement. In the opinion of the Tribunal the payments made to SWCL in the form of royalty was for use of technical know-how and experience of SWCL. The assessee not having acquired any asset of enduring nature the payment could not be termed as a capital expenditure. In the background of these findings, the Tribunal held that the Assessing Officer was not justified in applying the provisions of Section 35A of the I.T. Act.

15. In so far as the applicability of the provisions of Section 40A(2) of the I.T. Act was concerned, the Tribunal was of the view that the Assessing Officer had failed to bring any evidence on record that SWCL held majority shares in the assessee. In this connection the Tribunal also noticed that the revenue was obliged to show that SWCL either held 20% or more of the shares (including right to receive dividend) or 20% or more of the voting rights in the assessee. The Tribunal deprecated the approach adopted by the Assessing Officer, which according to it, was not backed by cogent findings that SWCL had a substantial interest in the assessees business. The Tribunal after noticing the divergent views expressed by the CIT(A) in assessment year 1998-1999 as against those taken in 1997-1998 and 1999-2000, approved the view of the CIT(A) taken in assessment year 1998-1999, including the reasoning given therein.

16. On the aspect of the difference in bottling charges paid to the assessee, as against those paid to one Balbir, Distilleries Ltd. by SWCL; in paragraph 29, the Tribunal accepted the rationale provided by the assessee that at the time at which SWCL had entered into a bottling agreement with Balbir Distilleries Ltd. it did not have the necessary facilities for the said purpose in the North India; therefore, in order to establish its presence in North India it ended up paying higher bottling charges to Balbir Distilleries ltd.

16.1 That apart the Tribunal was persuaded by the explanation given by the assessee that given the fact that Balbir Distilleries Ltd. had a plant of a much lower capacity, as compared to that of the assessee which had a capacity which was four times the capacity of Balbir Distilleries ltd.; the unit charges claimed by Balbir Distilleries Ltd. would naturally be higher in comparison to those claimed by the assessee since, the variable cost per unit in the case of the assessee would be appreciably lower given its capacity for higher production, and that this would also be true of fixed overheads which were again apportioned on, larger production, generated in case of assessee.

16.2 The Tribunal also noticed that the assessee had two bottling lines, while Balbir Distilleries Ltd. had only one bottling line.

16.3 For all these reasons, the Tribunal came to the conclusion that the royalty paid by the assessee to SWCL was neither excessive nor unreasonable and hence invocation of the provisions of Section 40A(2)(a) by the Assessing Officer was unjustified and, thus, the disallowance had to be deleted. The Tribunal thus upheld the order of the CIT(A) for assessment year 1998-99 and directed the Assessing Officer to apply the same in respect of assessment years 1997-98 and 1999-2000 also.

17. Before us arguments on behalf of the revenue have been advanced by Ms Rashmi Chopra, Advocate and those on behalf of the assessee by Mr Ajay Vohra, Advocate.

17.1 In support of the appeals filed by the revenue Ms Rashmi Chopra has largely relied upon the orders passed by the Assessing Officers in the concerned assessment years. More specifically, Ms Rashmi Chora argued, based on the terms and conditions contained in the said agreement that the assessee had acquired right to use the brands and the trademarks referred to in Appendix „C of the said agreement, and hence the payments made SWCL towards royalty were in the nature of capital expenditure. It was the contention of Ms Rashmi Chopra that in clause 6.3 of the agreement there is a reference to a separate agreement; an agreement which the assessee did not supply and hence, an adverse inference ought to be drawn against the assessee. To buttress her contention that the

payments made for use of trademark and brand names were in the nature of capital expenditure, reliance was placed on the observations made by this court in CIT Vs J.K. Synthetics (2009) 309 ITR 371 in paragraph 58 at page 414.

17.2 In so far as the invocation of provisions of Section 40A(2) was concerned, Ms Rashmi Chopra submitted that the Assessing Officer had noticed in paragraph 2 of his order dated 27.03.2000, passed in respect of assessment year 1997-1998, that shares in the assessee had been acquired by six (6) entities; and thus according to her the SWCL group had substantial interest in the assessee. She submitted that if this was so then the conclusion of the Tribunal that the provisions of Section 40A(2)(b) were not attracted, is erroneous.

17.3 It may, however, be noted here that Ms Rashmi Chopra did contend that the Assessing Officer had returned no finding as to the exact shareholding interest, and thereby, the extent of voting power acquired by SWCL in the assessee. She submitted that the Assessing Officer had admittedly only referred to the number of shares held by the six (6) entities in SWCL without taking the exercise to its logical conclusion. She thus submitted that the Tribunal being the final fact finding authority, it ought to have undertaken this exercise.

18. At this stage we may notice that we had put to Ms Rashmi Chopra, as to whether the revenue was required to take a stand at the beginning of the assessment proceedings as to the nature of the expenditure involved. As noticed by us hereinabove, the Assessing Officer in the same breath has categorized the sums paid by the assessee to SWCL in the form of royalty both as capital as well as revenue expenditure. After making such diametrically opposite observations, in each of the assessment years, the Assessing Officer has finally disallowed a substantial portion of the claim of the assessee by taking recourse to the provision of Section 35A of the I.T. Act. Consequently, in each of the assessment years in issue, only 1/14th of the expenditure, was allowed. This disallowance, by the Assessing Officer, is decidedly done on the basis that the expenditure in issue is in the nature of capital expenditure.

18.1 Ms Rashmi Chopra even while reluctantly conceding that there was perhaps an element of contradiction, submitted that she had no choice but to adopt the line

of reasoning reflected in the order passed by the Assessing Officer. We find this approach inexplicable. The reason for this being: in the assessment years 1998-99 the CIT(A) has taken this approach of the Assessing Officer to absurd length by bifurcating the disallowance to the extent of ` 24,70,929/- under Section 40A(2) and a balance sum equivalent to ` 55,06,643/- under Section 35A of the I.T. Act. Resultantly, the disallowance sustained by the CIT(A) is more than that which was quantified by the Assessing Officer.

19. Mr. Vohra, who appeared on behalf of the assessee submitted that the provisions of Section 35A of the I.T. Act were not attracted since there was neither acquisition of a patent nor any copyright. It was learned counsels submission that the assessee had acquired, if at all, only the use of trademarks and brand names of SWCL. He further submitted that in any event, the expenditure incurred, in the form of royalty paid to SWCL was in the nature of revenue expenditure and therefore, even on this ground the provisions of Section 35A of the I.T. Act were not attracted. On the other aspect as to whether the expenditure incurred by the assessee by way of royalty was excessive or unreasonable, having regard to the fair market value of the goods in issue, it was the learned counsels say that in order to attract the provisions of the said section, the conditionalities provided therein had to be fulfilled.

19.1 Mr. Vohra submitted that ordinarily expenses incurred by the assessee in connection with his business or profession had to be allowed notwithstanding the alleged imprudence of such expenditure from the point of view of the Assessing Officer. The expenditure incurred was amenable for deduction under the provisions of section 37 of the I.T. Act. The Assessing Officer if at all obtained jurisdiction to disallow a certain part of the expenditure on the ground that it was either excessive or unreasonable having regard to the fair market value of the goods, services or facilities in issue or by applying the test of legitimate needs of business or profession of the assessee or the benefit derived by or accruing therefrom to the assessee by virtue of the provisions of section 40A of the I.T. Act. In order to trigger the provisions of Section 40A(2)(a) of the Act, the person to whom such payments have been made by the assessee had to fulfill the test of proximity either by way of relationship or interest as provided in section 40A(2)(b)

read with the explanation appended to sub section (2)(b). Mr. Vohra submitted that the Assessing Officer in this regard had relied upon the provisions of section 40A(2)(b)(iv) read with the explanation. According to Mr. Vohra, a bare reading of the said provisions would indicate, that the Assessing Officer would have jurisdiction to disallow a portion of the expenditure incurred by the assessee only if, in the facts of the present case, it could have shown that SWCL had a demonstrable substantial interest in the business of the assessee. The substantial interest as has been defined in the explanation would require either a direct interest or a beneficial interest in atleast 20% of the voting power attached to the share holding or a share of not less than 20% in the profits of the business of such an assessee. Mr. Vohra submitted that the Assessing Officer in none of the years has returned a finding which fulfills the requirement of substantial interest as contained in section 40A(2)(b)(iv) read with the explanation. Therefore, it was contended, as rightly found by the Tribunal in the impugned judgment, that the provisions of section 40A(2)(a) not having been triggered, the disallowance under the said provision was not permissible.

20. We have heard the learned counsels for the parties. According to us, the appeal deserves to be dismissed for the reasons which are articulated hereinafter. But before we do that we must advert to one aspect of the matter to which reference has been made by us hereinabove. This aspect which we seek to refer to, is the contrary stands taken by the revenue, in respect of the nature of the expenditure involved. The revenue was required to first determine the nature of the expenditure and then assess for itself the relevant provisions which ought to have been invoked if at all to deny the deduction claimed by the assessee. The revenue on the other hand has tried to straddle two boats at the same time. In this regard, the Assessing Officer in the assessment year 1997-1998 while observing that the expenditure incurred by the assessee towards royalty was hit by the provisions of section 40A(2)(a), went on to ultimately disallow 13/14th part of the expenditure incurred, in the said assessment year, by taking recourse to section 35A of the Act. The CIT (A) in the said assessment year i.e., Assessment Year 1997-1998 bifurcated the disallowance by invoking both the provisions, that is, sections 40A(2)(a) and Section 35A. The result was that the disallowances crystallized by the CIT (A) was higher than that which had been made by the

Assessing Officer.

21. In the subsequent assessment years (i.e., 1998-1999 and 1999-2000) the Assessing Officer and in assessment year 1999-2000 has ultimately disallowed a part of the expenditure by invoking the provisions of section 35A of the I.T. Act; the only exception being the order of CIT(A) in assessment year 1998-1999. Therefore, we would first like to deal with the revenues stand that the expenditure had to be disallowed partially that is to the extent of 13/14 th by taking recourse to section 35A. Sub-section (1) of Section 35A requires broadly three (3) conditionalities to be fulfilled for it to be triggered:-

(i) the expenditure ought to have been incurred after 28.02.1966;

(ii) the expenditure should be related to acquisition of patent rights or copyrights used for the purposes of business;

(iii) lastly, the expenditure should be in the nature of capital expenditure.

22. In the instant case, we have no hesitation in saying that the expenditure incurred by the assessee was neither for acquisition of any patents or copyrights. This is not even the case of the revenue.

The revenue has latched on to royalty paid for use of trademarks and brands of SWCL. It was agued by Ms. Rashmi Chopra, learned counsel for the revenue that the expenses incurred for use of trademark ought to be treated as capital expenditure. In this regard, the learned counsel has relied upon a judgment of Division Bench of this court in the case of CIT v. J.K. Synthetics Ltd (supra).

22.1 On a reading of the judgment, we do not find any observation which could support the submissions made by the assessee. The broad principles as gleaned from various rulings of the Supreme Court and the High Courts have been noted at page 412 in paragraph 55 of the report. There is nothing to suggest in the principles referred to therein which would support the contention of the learned counsel for the revenue that a mere use of trademark or brand name would give colour to the expenditure incurred as if, it was on capital account. As a matter of fact principles (v) and (vi) adverted to at pages 412 & 413 run completely counter

to the submission made on behalf of the revenue. For the sake of convenience the same are extracted hereinafter.

"(v) expenditure incurred for grant of License which accords "access" to technical knowledge, as against, "absolute" transfer of technical knowledge and information would ordinarily be treated as revenue expenditure. In order to sift, in a manner of speaking, the grain from the chaff, one would have to closely look at the attendant circumstances, such as:

(a) the tenure of the licence.

(b) the right, if any, in the licensee to create further rights in favour of third parties,

(c) the prohibition, if any, in parting with a confidential information received under the license to third parties without the consent of the licensor,

(d) whether the licence transfers the "fruits of research" of the licensor, "once for all",

(e) whether on expiry of the licence the licensee is required to return back the plans and designs obtained under the licence to the licensor even though the licensee may continue to manufacture the product, in respect of, which "access" to knowledge was obtained during the subsistence of the licence.

(f) whether any secret or process of manufacture was sold by the licensor to the licensee. Expenditure on obtaining access to such secret process would ordinarily be construed as capital in nature;

(vi) the fact that assessee could use the technical knowledge obtained during the tenure of the license for the purposes of its business after the Agreement has expired, and in that sense, resulting in an enduring advantage, has been categorically rejected by the courts. The Courts have held that this by itself cannot be decisive because knowledge by itself may last for a long period even though due to rapid change of technology and huge strides made in the field of science, the knowledge may with passage of time become obsolete;"

22.2 The observation made in paragraph 58 at page 414 of the aforementioned judgment, on which reliance has been placed by the learned counsel for revenue seeks only to emphasise that the assessee in that case, had only acquired access to technology which was not related to any secret process or patent rights and thus in continuum it is mentioned that not even a right to use the trademark or brand name had inhered in the assessee. From this, it cannot be concluded, as is sought to be done by the learned counsel for the revenue that any payment made for use of trademark or trade name ipso facto will give colour to the payment as if it is made on capital account. This is in our view is a complete mis-reading of the judgment. It is well settled that a judgment is an authority for what it decides and not what is construed as logically flowing from it. Judgments cannot be read as statutes. A stray sentence picked out of context, cannot be used to turn its ratio around.

22.3 We have already referred to the provisions of the agreement. A perusal of the provisions of the agreement would show all that the assessee acquired was the use of the brand names and the trade marks of SWCL, which find a mention in Appendix-C annexed to the said agreement. The assessee acquired no right to any secret process or formulate or even any right title and interest in the trade marks and brands under which the IMFL products were sold. As a matter of fact assessees rights were co-terminus with the subsistence of the said agreement. Therefore, we have no hesitation in rejecting the contention of the revenue in this regard. On this issue Ms Rashmi Chopra had referred to the fact that the copy of the separate agreement had not been supplied by the assessee and, therefore, Tribunal ought to have drawn an adverse inference against the assessee. To test the veracity and seriousness of this submission we had called upon Ms Rashmi Chopra to show from the record whether such a ground had been taken in either their appeal filed before the Tribunal against the order of CIT(A) for assessment year 1998-99 or in the appeal filed before us. Ms Rashmi Chopra was unable to refer to any such ground. It is quite evident that the Revenue took the stand, though erroneously, that royalty paid on use of brand names and trade marks would classify the expenditure as one made on capital account.

23. This brings us to the issue as to whether the Assessing Officer could have invoked the provisions of section 40A(2)(a) of the Act in the facts and circumstances of the present case. As is noticed in the earlier part of our judgment, the Assessing Officer in the assessment year 1997-1998 after recording that the shares of the assessee were held by six (6) entities goes on to observe that the assessee "became a subsidiary of Shaw Wallace Group of Companies". There is no finding recorded by the Assessing Officer that SWCL had acquired substantial interest i.e., 20% or more of the share capital with attending voting rights, whether directly or beneficially. If that is so, then the provisions of section 40A(2)(a) could not have got triggered.

It is noticed that the CIT (A) in the assessment year 1998-1999 has returned a finding that there were five (5) limited companies apart from two (2) individuals who held shares in the assessee, but none of the entities adverted to, by the Assessing Officer, both in the assessment year 1997-1998 and 1998-1999 is SWCL. As a matter of fact, the CIT (A) in assessment year 1998-1999 records that not a single share in the assessee is held by SWCL. The CIT (A) further records a finding of fact that, on a perusal of list of shareholders, it is clear that even the employees of SWCL did have ownership of a controlling share holding interest in the assessee. CIT(A) records that six (6) individuals held ten (10) shares each in the assessee while, one gentleman by the name of Mr. Suraj P. Gupta held 8,61,610 shares who was neither an employee of the assessee and nor was any payment made to Mr. Suraj P. Gupta or his relative or to a company of which he was a Director. The CIT (A) went on to hold that, in the instant case, payments had not been made to persons specified under section 40A(2)(b) and therefore, the provisions of section 40A(2) were not applicable. Both CIT (A) as well as the Tribunal have also accepted the explanation given by the assessee with regard to difference in payment of bottling charges vis-à-vis Balbir Industries Limited and the assessee. The reference to which we have already made hereinabove. We find no perversity in the findings of the Tribunal and those recorded by CIT(A) in assessment year 1998-1999.

24. Therefore, for the foregoing reasons, we are of the view that the Tribunal in the impugned judgment and the CIT (A) in its order dated 15.05.2000 passed in the

Assessment Year 1998-1999 has correctly appreciated the provisions of section 40A(2) of the I.T. Act thus the contention of the revenue even on this aspect has to be rejected.

25. In our considered opinion, the matter raises pure findings of fact. There are no questions of law much less substantial questions of law which require our consideration. The appeals are accordingly dismissed.