Bombay High Court Deputy Cit vs Metro Shoes (P) Ltd. on 9 August, 2002 Equivalent citations: (2004) 89 TTJ Mumbai 48 ORDER A.K. JA.IN, J.M.: This appeal has been filed by the department against the order dated 4th Aug., 1994, of the learned Commissioner (Appeals)-XlI, Bombay, for the assessment year 1991-92. 2. The department has raised the following grounds of appeal. "1. On the facts and in the circumstances of the case and in law, the learned Commissioner (Appeals) erred in holding that expenditure of Rs. 2.80 lakhs incurred on telefilin is allowable as revenue expenditure disregarding the fact that asset acquired with enduring benefit was to be used for the purpose of advertisement of business. also should have followed the ratio of the decision laid down by the Bombay High Court in the case of CIT v. Patel International Film ITD. (1976) 102 ITR 219 (Bom)."2. On the facts and in the circumstances of the case and in law, the learned Commissioner (Appeals) erred in deleting addition amounting to Rs. 28,117 disregarding the fact that object of expenditure incurred on account of stamp duty related to acquisition of asset and is assessable under Capital Head." 3. The assessee-company is a trader in footwear and leather products like shoes, hand-bags, etc. The assessee-company has various sales outlets throughout the country. It markets its shoes and other leather items at a selling price which includes a gross profit of 35 per cent. The sales outlets belong to different parties who are not connected with the assessee. These sales outlets are known as franchise shops, which get a commission of 20.5 per cent on the sales effected by them. If the shop owners make their own arrangements for their franchise shops, furniture and fixture, only then they are entitled for 20.5 per cent sales commission. If the assessee, i.e., Metro Shoes (P) ITD. invests in franchise shops, with furniture and fixture, the franchise shop owners are entitled for a commission of 17.5 per cent. This percentage varies in different shops. For example, in the case of a franchise shop at Connaught Place, Delhi, the percentage of profit is 7 per cent. In this case, the assessee pays 5 1/2 per cent as commission to the sales manager who looks after the sales of the shop. 3. The assessee-company is a trader in footwear and leather products like shoes, hand-bags, etc. The assessee-company has various sales outlets throughout the country. It markets its shoes and other leather items at a selling price which includes a gross profit of 35 per cent. The sales outlets belong to different parties who are not connected with the assessee. These sales outlets are known as franchise shops, which get a commission of 20.5 per cent on the sales effected by them. If the shop owners make their own arrangements for their franchise shops, furniture and fixture, only then they are entitled for 20.5 per cent sales commission. If the assessee, i.e., Metro Shoes (P) ITD. invests in franchise shops, with furniture and fixture, the franchise shop owners are entitled for a commission of 17.5 per cent. This percentage varies in different shops. For example, in the case of a franchise shop at Connaught Place, Delhi, the percentage of profit is 7 per cent. In this case, the assessee pays 5 1/2 per cent as commission to the sales manager who looks after the sales of the shop. The sales manager has to appoint his own staff. The goods lying at various, sales outlets is reflected in the closing stock. No shops are owned by the assessee. The sales are through franchise shops. 4. The assessee-company filed its return of income for assessment year 1991-92 admitting income of Rs. 9,83,160. The return was processed under section 143(1)(a) on income of Rs. 9,83,160. 4. The assessee-company filed its return of income for assessment year 1991-92 admitting income of Rs. 9,83,160. The return was processed under section 143(1)(a) on income of Rs. 9,83,160. During the assessment year 1991-92, the assessee has produced a video film for advertising of its products on television. The total cost of the production of the film amounted to Rs. 2.8 lakhs. The assessee was asked to show-cause as to why this expenditure should not be treated as capital expenditure. The assessee gave the following explanation : "The Supreme Court has, in the case of Assam Bengal Cement Co. ITD. v. CIT (1955) 27 ITR 34 (SC), enunciated broad tests so as to determine whether the amount of expenditure is of revenue nature or capital nature. These broad tests are as under : 1. Outlay is deemed to be capital when it is made for the initiation of a business, for extention of a business, or for a substantial replacement of equipment. 2. Expenditure may be treated as properly attributable to capital when it is 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. The enduring benefit or the right having enough durability to justify its being treated as a capital asset. 3. Whether the expenditure incurred was a part of fixed capital of the business or a part of its circulating capital." It can be appreciated that expenditure incurred for producing of film for advertisement does not pass any of the above tests and as such it has to be treated as of revenue nature. The said principles were again followed by the Supreme Court in the case of Empire Jute Co. ITD. v. CIT (1980) 17 CTR (SC) 113: (1980) 124 ITR 1 (SC) and by the Gujarat High Court in the case of CIT v. Shri Dig Way Cement Co. ITD. (1986) 53 CTR (Guj) 274 : (1986) 159 ITR 253 (Guj). On a point similar to the one in question the Tribunal, Ahmedabad Bench 'A', has in the case of LAC v. Joshi Formulebs (P) ITD. (ITA No. 3385/Ahd/1987) held has that the expenditure on the production of advertisement film is a revenue expenditure. 6. The learned assessing officer, vide the assessment order held 6. The learned assessing officer, vide the assessment order held Normally, the expenditure incurred on advertisement is of revenue nature and is allowable if it does not fall within any specific statutory provision. But if a capital asset is purchased which is employed for advertisement purpose, it is a capital expenditure. In CIT v. Patel International Film ITD. (supra), the assessee, a movie processing and printing concern, purchased a film which was processed in its own laboratory and used it to serve as a nodal for exhibition by way of advertisement. It was held that that the expenditure was of capital nature. Under the circumstances the expenditure of Rs. 2,80,000 incurred for production of telefilm is considered as a capital expenditure and not allowed as a revenue expenditure. The depreciation as per the rate applicable is allowed. 7. It is this addition which forms the basis of first ground of appeal. 7. It is this addition which forms the basis of first ground of appeal. 8. In the appeal before the Commissioner (Appeals), the assessee alleged, inter alia, that advertisement films, which are produced for advertising the products on television and video do not have a very long life and normally, these films are to be replaced after 6 to 9 months and new films have to be circulated thereafter; that no assets of permanent nature or right or benefit of enduring nature is created when an advertisement film is produced and hence cost thereof should not have been treated as capital expenditure; and that as per the broad test laid down by the Hon'ble Supreme Court to decide whether the expenditure is capital or revenue nature, this ought to have been treated as a revenue nature. 8. In the appeal before the Commissioner (Appeals), the assessee alleged, inter alia, that advertisement films, which are produced for advertising the products on television and video do not have a very long life and normally, these films are to be replaced after 6 to 9 months and new films have to be circulated thereafter; that no assets of permanent nature or right or benefit of enduring nature is created when an advertisement film is produced and hence cost thereof should not have been treated as capital expenditure; and that as per the broad test laid down by the Hon'ble Supreme Court to decide whether the expenditure is capital or revenue nature, this ought to have been treated as a revenue nature. 9. By virtue of the impugned appellate order, the learned Commissioner (Appeals) observed, amongst other things, that by production of an advertisement film, the life of which. is 6 to 9 months it cannot be said that the assessee tried to acquire a capital asset; that moreover, the expenditure is for meeting the day-to-day running of business of the assessee and not for acquiring business asset itself; that, therefore, the decision cited by the learned assessing officer (CIT v. Patel International Filrn ITD. (supra)l is not applicable to the present case; that the decision of CIT v. Shn Dig Way Cement Co. ITD. (supra) is applicable along with the decision of the Tribunal, Ahmedabad Bench W, in the case of LAC v. Joshi Formulabs (P) ITD. (supra) where the Tribunal held on facts that the film became useless in a period of less than two years which indicated that the advertisement film does not result in any enduring benefit to the assessee. The addition was, therefore, deleted. 9. By virtue of the impugned appellate order, the learned Commissioner (Appeals) observed, amongst other things, that by production of an advertisement film, the life of which. is 6 to 9 months it cannot be said that the assessee tried to acquire a capital asset; that moreover, the expenditure is for meeting the day-to-day running of business of the assessee and not for acquiring business asset itself; that, therefore, the decision cited by the learned assessing officer (CIT v. Patel International Filrn ITD. (supra)l is not applicable to the present case; that the decision of CIT v. Shn Dig Way Cement Co. ITD. (supra) is applicable along with the decision of the Tribunal, Ahmedabad Bench W, in the case of LAC v. Joshi Formulabs (P) ITD. (supra) where the Tribunal held on facts that the film became useless in a period of less than two years which indicated that the advertisement film does not result in any enduring benefit to the assessee. The addition was, therefore, deleted. 10. It has been submitted before us by the learned departmental Representative that since the benefit derived from the production of the film is of enduring nature the expenditure on the production of such advertising film is a capital expense. 10. It has been submitted before us by the learned departmental Representative that since the benefit derived from the production of the film is of enduring nature the expenditure on the production of such advertising film is a capital expense. 11. On the other hand, the learned representative for the assessee, besides broadly repeating the arguments raised before the authorities below, has submitted that the expenditure in question is an allowable expenditure under section 37(1) of the Income Tax Act being a revenue expenditure in nature. A note has been submitted which gives the facts on the point and reiterates the stand of the assessee. 11. On the other hand, the learned representative for the assessee, besides broadly repeating the arguments raised before the authorities below, has submitted that the expenditure in question is an allowable expenditure under section 37(1) of the Income Tax Act being a revenue expenditure in nature. A note has been submitted which gives the facts on the point and reiterates the stand of the assessee. 12. It has been stated that by making up the film, no new asset of durable nature or right has been created. In the present world, fashion changes rapidly. So, any advertisement, may it be by any mode, including by way of an advertisement film, such advertisement looses value quickly at the most within 6 to 9 months of its release. It has thus been averred that the cost of production of the advertisement film of the assessee should not be capitalised. 12. It has been stated that by making up the film, no new asset of durable nature or right has been created. In the present world, fashion changes rapidly. So, any advertisement, may it be by any mode, including by way of an advertisement film, such advertisement looses value quickly at the most within 6 to 9 months of its release. It has thus been averred that the cost of production of the advertisement film of the assessee should not be capitalised. 13. An alternative argument has also been raised by the assessee to the effect that even under section 37(3) of the Income Tax Act, this expense deserves complete deduction. 13. An alternative argument has also been raised by the assessee to the effect that even under section 37(3) of the Income Tax Act, this expense deserves complete deduction. 13.1 Distinguishing the judgment of the Hon'ble Bombay High Court in the case of CIT v. Patel International Film (P) ITD. (supra), it has been stated that the facts of that case were entirely different from those attending here. There, it was a case of full length feature film processing, the purchase of a capital asset was involved. Contrary, the assessee here is not in the business of advertisement. So, it has been insisted that reliance on the said judgment has wrongly been placed by the assessing officer to the detriment of the assessee. 13.1 Distinguishing the judgment of the Hon'ble Bombay High Court in the case of CIT v. Patel International Film (P) ITD. (supra), it has been stated that the facts of that case were entirely different from those attending here. There, it was a case of full length feature film processing, the purchase of a capital asset was involved. Contrary, the assessee here is not in the business of advertisement. So, it has been insisted that reliance on the said judgment has wrongly been placed by the assessing officer to the detriment of the assessee. 13.2 The assessee has, then placed reliance on the decision of the Tribunal, Ahmedabad Bench W, in the case of LAC v. Joshi Formulabs (P) ITD. (supra). A copy of the said order has been placed on record. 13.2 The assessee has, then placed reliance on the decision of the Tribunal, Ahmedabad Bench W, in the case of LAC v. Joshi Formulabs (P) ITD. (supra). A copy of the said order has been placed on record. 14. Having heard both the parties at length and having gone through the record of the case, we do not find any reason whatsoever to interfere with the order of the learned Commissioner (Appeals). Undeniably, no capital asset or right or benefit of enduring nature has been created or acquired by the assessee by production of the advertisement film in question. It is common knowledge that public interest, like public memory, has a short span of life. In order to keep mass interest intact in its products an assessee has to continuously strive to keep on advertising their products in ever increasingly novel ways and methods, through the media. This involves a continuous change in the advertisement of the products. So as to catch and hold the interest of the consumer, the assessee has to keep on launching new products, for which new advertisements have to be floated. This itself makes it clear that an advertisement film ordinarily does not have a life of more than a year at the maximum. Such films are definitely covered by the settled Economic principles of diminishing marginal utility. Their value goes on decreasing with the passage of time. That being so, there is no question of the present assessee having acquired any capital asset or right or benefit of enduring nature. Hence, one is led but to the conclusion that the expenditure incurred an the production of the advertisement film was in the nature of a revenue expenditure, which should not have been capitalised. 14. Having heard both the parties at length and having gone through the record of the case, we do not find any reason whatsoever to interfere with the order of the learned Commissioner (Appeals). Undeniably, no capital asset or right or benefit of enduring nature has been created or acquired by the assessee by production of the advertisement film in question. It is common knowledge that public interest, like public memory, has a short span of life. In order to keep mass interest intact in its products an assessee has to continuously strive to keep on advertising their products in ever increasingly novel ways and methods, through the media. This involves a continuous change in the advertisement of the products. So as to catch and hold the interest of the consumer, the assessee has to keep on launching new products, for which new advertisements have to be floated. This itself makes it clear that an advertisement film ordinarily does not have a life of more than a year at the maximum. Such films are definitely covered by the settled Economic principles of diminishing marginal utility. Their value goes on decreasing with the passage of time. That being so, there is no question of the present assessee having acquired any capital asset or right or benefit of enduring nature. Hence, one is led but to the conclusion that the expenditure incurred an the production of the advertisement film was in the nature of a revenue expenditure, which should not have been capitalised. 15. In view of the above discussion, this issue is decided in favour of the assessee and against the department. The main argument having thus been dealt with, we do not deem it necessary to go into the alternative submissions of the assessee. 15. In view of the above discussion, this issue is decided in favour of the assessee and against the department. The main argument having thus been dealt with, we do not deem it necessary to go into the alternative submissions of the assessee. 16. The second issue pertains to the addition of Rs. 28,117 incurred on account of stamp duty. A perusal of the opening sentence of the assessment order pertaining to the point in issue shows that this expenditure was incurred by the assessee for the purpose of acquiring certain assets on lease from M/s Forward Leasing & Electronics in February, 1987. As a part of the agreement, 20 bills of exchanges were drawn, promising the payment of Rs. 1;62,240 in respect of each of the bills after certain dates. Stamp duty amounting to Rs. 28,117 was affixed on these bills of exchanges. The assessee's lease agreement could not come through and, therefore, the bills of exchange became redundant. The assessee- company tried to recover the money of the stamp duty from the stamp duty authority during the period 1987 to March, 1991. But, ultimately, the company received a final reply from the stamp authorities in March, 1991, stating that the stamp duty paid amounting to Rs. 28,117 cannot be refunded. Therefore, the assessee claimed this expenditure in the P&L account for assessment year 1991-92. The assessing officer held that this expenditure is not an allowable business expenditure. Since the stamp duty is incurred in connection with the acquisition of a capital asset; that the stamp duty forms a part of the capital expenditure and hence it cannot allowed as a revenue expenditure; and that also once the assessee incurred the amount of Rs. 28,117 in February, 1987, which falls in the assessment year 1987-88, the assessee should have claimed this expenditure in that year. Thus, this stamp duty of Rs. 28,117 was disallowed and added back to the income of the assessee as capital expenditure and prior year expenses. 16. The second issue pertains to the addition of Rs. 28,117 incurred on account of stamp duty. 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Before the learned Commissioner (Appeals), it was submitted on behalf of the assessee: "Expenditure on raising loans : A loan obtained cannot be treated as an asset or advantage for the enduring benefit of the business of the borrower. A loan is a liability and has to be repaid and it is erroneous to consider a liability as an asset or an advantage far less of an enduring nature. Expenditure incurred for or in raising a loan for the purpose of the business is not in the nature of capital expenditure and is laid out or expended wholly and exclusively for business purposes (India Cements ITD. v. CIT (1966) 60 ITR 52, 62 (SC)) and Rampoolla Cotton Mills ITD. v. CIT (1974) Tax LR 395 (Cal)). The purpose for which the loan was required is irrelevant to the consideration of the question whether the expenditure for raising loan is revenue expenditure or capital expenditure. (Nagpur Electric Light & Power Co. v. CIT (1931) 6 ITC 28 (Nag Jud. Comnir.)J, approved in this respect, by the Supreme Court in India Cements' case (supra)). Whether capital or revenue? The very word 'loan' implies a liability and it is difficult if not impossible to conceive of a loan as something which brings into existence an asset of an enduring nature. Expenditure incurred for stamp and registration charges for entering into an agreement with a bank for overdraft facilities for the purpose of business is on revenue account and allowable (Ishwari Khetan Sugar Mills (P) ITD. v. CIT (1967) 63 ITR 376 (All)). Which expenses are deductible ? Expenditure incurred on stamps, registration fees, charges for certified copy of the mortgage deed, indemnity deed, lawyers' fees for drafting the deed and legal fees payable in connection with raising a business loan not of capital nature are laid out or expended wholly and exclusively for the purpose of the taxpayer's business and are allowable under these provisions (India Cements ITD. v. CIT (1966) 98 In 20 (SC)), Prem Spg. & Wvg. Mills Co. ITD. v. CIT (1975) 98 17R 20 (All), also see Western India Ofl Dist. Co. ITD. v. CIT (1979) 77 ITR 140 (Bom)). Similarly, legal charges incurred in obtaining a loan for certain period (as opposed to it being an asset or advantage of an enduring nature) are allowable under these provisions irrespective of the object with which the loan was obtained (Orissa Cement ITD. v. CIT (1969) 73 ITR 14, 19 (Del)). Expenses on overdraft facilities : In India Cement ITD. v. CIT (1966) 60 ITR 52 (SC)), the Supreme Court held that the expenditure incurred by the assessee for obtaining a loan from the industrial finance corporation secured by a charge on its fixed assets was an admissible allowance, because the act of borrowing the money was incidental to the carrying on of business and that it was irrelevant to consider the object with which the loan was obtained. In JeewanIal (1929) ITD. v. CIT (1969) 74 ITR 753 (SC)), the Supreme Court applied those principles to hold that the expenditure incurred to secure overdraft facilities with bank for the purpose of assessee's business was of a revenue nature and allowable under these provisions irrespective of the period for which it was granted or the terms whereon it was obtained. (Also see, Ishwari Khetan Sugar Mills (P) ITD. v. CIT (supra) and Orissa Cement ITD. v. CIT (supra) The learned Commissioner (Appeals) deleted the addition. The learned departmental Representative has simply stated that since the expenses on stamp duty were incurred in connection with the acquisition of a capital asset, stamp duty formed a part of capital expenditure and was not allowable as a revenue expenditure. 18. The learned departmental Representative has sought to rely on the following judgments to butress his stand that stamp duty paid on documents for assets proposed to be taken on lease basis is deductible as revenue expenditure. 18. The learned departmental Representative has sought to rely on the following judgments to butress his stand that stamp duty paid on documents for assets proposed to be taken on lease basis is deductible as revenue expenditure. (i) CIT v. Hoechst Phannaceuticals ITD. 1978 CTR (Bom) 523 (1978) 113 ITR (ii) Richardson Hindustan ITD. v. CIT (1987) 63 CTR (Bom) 16 (1988) 169 ITR 516 (Bom) (iii) CIT v. Burroughs Wellcome & Co. (India) (P) ITD. (1981) 23 CTR (Bom) 102 (1982) 133 ITR 37 (Bom) (iv) CIT v. Cinceita (P) ITD. (1982) 28 CTR (Bom) 250 : (1982) 137 ITR 652 (Bom) (v) CIT v. Bombay Cycle & Motor Agency ITD. (1979) 12 CTR (Bom) 243: (1979) 118 ITR 42 (Bom). 19. Admittedly, the stamp duty was affixed on 20 bills of exchanges, which were drawn, promising the payment of Rs. 1,62,240, pertaining to buying of certain assets on lease from M/s Forward Leasing & Electronics. 19. Admittedly, the stamp duty was affixed on 20 bills of exchanges, which were drawn, promising the payment of Rs. 1,62,240, pertaining to buying of certain assets on lease from M/s Forward Leasing & Electronics. 20. It is well settled that when the transaction involved is a lease and not a purchase, the expenditure incurred thereon, including brokerage or commission or stamp duty or the like, this expenditure is allowable as a revenue expenditure. As such, the stand of the assessee is correct. So, the order of the learned Commissioner (Appeals) does not call for interference. Thus, it is confirmed. 21. As a result, the appeal of the revenue is dismissed. 20. It is well settled that when the transaction involved is a lease and not a purchase, the expenditure incurred thereon, including brokerage or commission or stamp duty or the like, this expenditure is allowable as a revenue expenditure. As such, the stand of the assessee is correct. So, the order of the learned Commissioner (Appeals) does not call for interference. Thus, it is confirmed. 21. As a result, the appeal of the revenue is dismissed.