Ford India (P) Ltd, Chennai vs Dy Cit Ltu, Chennai on 12 May, 2017

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IN THE INCOME TAX APPELLATE TRIBUNAL
'D' BENCH: CHENNAI

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BEFORE SHRI N.R.S. GANESAN, JUDICIAL MEMBER AND
SHRI D.S.SUNDER SINGH, ACCOUNTANT MEMBER

./ITA Nos.2344 & 2345/Mds/2012
* * /Assessment Year: 2005-06 & 2008-09

M/s.Ford India Pvt. Ltd., S.P.Koil Post, Chengalpattu-603 204.	Vs.	The Dy. Commissioner of Income Tax, Large Taxpayer Unit, Chennai.

[PAN: AAACM 4454 H]

(-/Appellant)	(./ -/Respondent)

- 0 / Appellant by	:	Mr.Arvind Sonde, Advocate
./ - 0 /Respondent by	:	Mr.Pathlavath Peeriya, CIT
0 /Date of Hearing	:	28.02.2017
i¢ 0 /Date of Pronouncement	:	12.05.2017

/ O R D E R

PER D.S.SUNDER SINGH, ACCOUNTANT MEMBER:

These appeals are filed by the assessee against the orders passed by the Dy.Commissioner of Income tax, Large Taxpayer Unit, Chennai u/s 143(3) r.w.s.144C/147 for the A.Y 2005-06 dated 29/10/2012 and for the A.Y 2008-09 on 29/10/2012. Since the common issues are involved in both the appeals, both are clubbed, heard together and disposed off in ITA Nos.2344 & 2345/Mds/2012 :- 2 -:

common order for the sake of the convenience. Since the facts of both the assessment years are identical the relevant information from the A.Y.2005-06 adopted for deciding the appeals.

2.0 Ford is one of the world's largest producers of passenger cars and trucks with manufacturing, assembly or sales operations in more than 200 markets in six continents. Ford India Pvt. Limited (FIPL) is a wholly owned subsidiary of Ford Motor Company, USA (FMC). In February 1995, Ford purchased 5.8% of Mahindra & Mahindra (M&M) and in September 1995, Ford and M&M sought the approval for establishing a joint venture company to manufacture and distribute vehicles and subsequently after getting the approval, the joint venture was established. In March 1998, the equity pattern changed to 70:30 with Ford having the majority stake and the company was renamed as Ford India Private Ltd. (FIPL). The equity pattern changed in various stages and finally in March 2005, the Ford International Services purchased the remaining shares from M&M, Thus FIPL became a wholly owned subsidiary of FMC. FIPL established its fully Integrated facility in Chennai in 1999.

2.1 During the assessment proceedings, the AO found the international transaction with the A.E for Rs.559.73 crores for the A.Y 2005-06 and Rs.835.83 Cr. for the A.Y 2008-09. The details of International transaction for the AY 2005-06 are reproduced here under:

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> Quantum of S. Details of International transactions International & No. Transactions (Rs.) 1 Export of auto components and service parts 1450298239 2 Import of Auto Components and Service parts 3831469511 3 Import of Cars 15932771 4 Fusion Technical Service Publication 4502764 5 Development cost of base manual 339708 6 Royalty 172524382 7 Technical training cost 172033 8 Reimbursement of expenses 114088961 9 Training and road show expenses 8025798 Total 5597354167 The AO has referred the international transactions to the TPO for determining the ALP. The company has reported three distinct activities namely -

• The Contract manufacturing activity • Distribution activity and • Entrepreneurial activity 2.2 Contract manufacturing involves a company (the entrepreneur) that produces the products to sell to its customers by hiring a provider of manufacturing services (the contract manufacturer) to actually make the products. The essence of the contract manufacturing activity is that the entrepreneur bears the primary financial risks and the market risks associated with competition and customer acceptance of the product. The contract manufacturer is merely a service provider that earns a service fee and bears no direct financial or market risks with respect to the product it manufacturers.

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> 2.3 The assessee has adopted the TNMM as the most appropriate method for the purpose of Transfer Pricing analysis of manufacturing activity done by the assessee company. For this purpose the assessee company has been selected as the tested party. The assessee company conducted a worldwide search based on foreign database like Disclosures Global Research - SEC, Computstat Data, Movies company Data Amadus;

FAME, etc. The search process using primary sources and secondary sources yielded thousands North American, European and Asian companies being identified as potentially engaged in contract manufacturing. Out of this, based on various criteria as filters, the number of contract manufacturers was restricted to reasonable numbers in the three markets mentioned above. The Arm's Length range for this analysis is based on the financial results for the previous years. The return on capital employed (ROCE) was chosen as the PLI. The assesses has also adopted OP to Cost as the alternative method to justify the Arm's Length. 2.4 In the case of distribution activity similar exercise was carried out. In the case of Ford company apart from its own domestic market, in case of other markets, the vehicles are sold to Ford affiliates called National Sales Companies. The primary function of an NSC is to use its Field Sales Force to call on the independent dealers. Accordingly the Ford NSC is functionally comparable to uncontrolled wholesale distributors doing business in many product Industries. A distributor is essentially here the service provider providing distribution services to its service provider to ITA Nos.2344 & 2345/Mds/2012 :- 5 -:

> earn mark up on its distribution cost and also a cost on its capital incurred. The tested party is the NSC. After conducting an independent search the assessee identified comparable companies in North America, Europe and Asia Pacific. Various adjustments were made by the assesses on inventory and accounts receivable. Other adjustments were made on advertising and other direct marketing expenses. The analysis were carried out during the earlier year periods. FAR analysis was also done on this activity.
>
> 2.5 There is no mention about the entrepreneurial segment of the assessee company's activities, even though the volume of sales of this segment is substantial. There is no FAR analysis or any description of the nature and scope of the activity and the methodology to be adopted for comparison with uncontrolled transactions.
>
> 2.6 The tested party adopted by the assessee in the case of both manufacturing activity and distribution activity is the assessee company itself, A tested party is the one which has the least complex operations.

The tested party is the participant in a related party transaction whose price is or whose profit margins will be tested using the most appropriate pricing method. The tested party is ordinarily the party whose prices or profits can be verified using the most reliable data and requiring the fewest and most reliable adjustments and for which reliable data regarding uncontrolled comparables can be located. The tested party will ITA Nos.2344 & 2345/Mds/2012 :- 6 -:

> not own valuable intangible property or unique assets that distinguish it from potential uncontrolled comparables. The assessee being the tested party, considering comparables in North America, Europe and Asia Pacific Region is not correct, as per the Income Tax Provisions. The tested party i.e. Ford India Pvt Ltd., being a resident Indian Company, comparable companies exclusively from India based on Indian data bases should be adopted.
>
> On a perusal of the TP document by the TPO, it was seen that the assessee company has taken comparables relating to the earlier period. No contemporaneous data relating to this financial year has been considered by the assessee. Moreover, the

comparables adopted by the assessee are all foreign companies which is not acceptable, to the TPO, since the Transfer Price arose during the course of transactions carried out by the resident company i.e., Ford India Private limited.

3.0 The TPO did not accept the TP study of the assessee for the reasons discussed in Para 2.6 above stating that the TP study conducted by the assessee is unreliable and unacceptable. An independent search was conducted by the TPO and four companies were identified as comparables as under:

S.No.	Name of the company	PLI
1	General Motors India Pvt. Ltd	-0.60%
2	Mahindra & Mahindra Ltd.	5.67%
3	Maruti Suzuki India Ltd	8.46%
4	Tata Motors Ltd.	6.52%
	Average	5.01%

and worked out the average margin of 5.01% of the comparables against the assessee's operating margin of (-)1.27%. Hence, the AO worked out the difference in ALP to Rs.122.62 Cr. In addition to the ALP difference the TPO proposed to make separate adjustment on account of brand building activities, advertisement expenses and product development expenses. Accordingly issued the show cause notice to the assessee and the assessee filed reply to the show cause notice objecting for the TP study made by the AO for substituting the single year data instead of multiple year data adopted by the assessee and for separate adjustments on account of brand building, product development, advertisement and marketing expenses and also sought for some economic adjustments. The TPO rejected the objections raised by the assessee and determined the ALP of Rs.1,744.24 Cr. and for the adjustment of Rs.122.62 Cr towards the ALP transactions for the AY 2005-06 as per the details given below:

Operating Income	16216171090
Operating cost	16424047843
Operating profit	-207876753
OP/Cost	-1.27
PLI of comparables	5.01%
ALP OP/Cost	6.28%
ALP Profit	1018375544
ALP Sales (Cost + ALP Profit)	17442423387
Difference	1226252297

Apart from the above the TPO suggested for the following adjustments:

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S.No.	Nature of adjustment	Amount in Rs. In crores
1	Arms length adjustment for international transactions	122.62
	Amount receivable by the assessee from the holding company for	16.32

building the brand and logo of the holding company to compensate the assessee for depriving it from developing a brand/logo legally and economically/owned by assessee. Amount towards advertisement and sales promotion expenses 52.23 incurred on behalf of the holding company with a purpose to promote business of the holding company, hence receivable by the assessee from the holding company Product development expenses to be recouped by Ford Motor 10.57 company Total 201.74 The AO issued draft Assessment Order proposing to make the TP adjustment as suggested by the TPO amounting to Rs.201.74 crores as above.

3.1 The assessee moved petition before the DRP against the draft Assessment Order u/s.144C of the Act. Before the DRP, the TPO raised the objections regarding the selection of comparables in respect of global entities and global approach for comparables and for exclusion of some of the comparables selected by the TPO, The AMP expenditure, brand development expenses and product development expenses. The DRP has observed that the TPO has made the adjustment both at the entity level as well as item wise adjustments towards AMP and product development expenses and brand development expenses. Hence, the DRP has confirmed the AMP, brand development and product development expenses and directed the TPO to exclude the entity level adjustment.

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Accordingly, the TPO has passed Modification Order No.F/101/TPO/1/AY 2005-06/RAV dated 16.10.2012 proposing to make the adjustment of Rs.79.12 Cr. as under:

AMP	52.32 Cr.
Brand development	16.32 Cr.
Product development	10.57 Cr.

However, TPO has specified a condition that in the event of deletion and addition of the above three adjustments, the margin adjustment of Rs.33.91 Cr. at the entity level will stay. Accordingly, the AO passed the orders u/s u/s.143(3) r.w.s.144C and 147 of Income Tax Act on 29.10.2012 incorporating the adjustment of Rs.79.12 Cr. on account of transfer pricing and other corporate additions. Against the order of the AO, the assessee is in appeal before us.

4.0 The assessee has raised 12 grounds in total in this appeal. Ground No.1 to 8 are related to the transfer pricing adjustments. In the transfer pricing the assessee raised the issues regarding, Global TP policy and segmentation, Comparability analysis and Margin adjustment, AMP, Brand Development fee and product development expenses, etc.., and argued at length.

5.0 We have heard the rival submissions and perused the material placed on record. On going through the DRP order in Page NO.4 the DRP has given the following Directions to the AO/TPO.

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> In addition to his report dated the 4th June' 2012 as mentioned above the Transfer Pricing officer also attended and participated during the course of the hearings before the Dispute Resolution Panel in terms of Order Sheet entry dated the 4th June, 2012 wherein he was in agreement with the adjustment detail given by the Eligible Assessee in terms of Annexure-C of its additional submissions before the Transfer Pricing Officer during the course of the proceeding before the Dispute Resolution Panel as detailed above. The Assessing authority and the Transfer Pricing Officer shall take any fresh position from those in the Transfer Pricing Order only after due verification of facts and contents and with full justification on merit.
>
> Consequently The TPO has passed an order on 16/10/2012 making amendment to the TPO's order u/s 92CA(3) dated 31/10/2011 substituting the entity level adjustment to Rs.33.91 crores and restricting the item wise adjustments of AMP, Brand Development and Product Development expenses and conveyed to the AO. The TPO also put a condition/ caveat in his amendment letter dated 16/10/2012 as under:
>
> A Condition/Cavcat is hence applicable in the context of the adjustments. The assessee Company will likely file Appeals before the ITAT or before higher legal authorities with respect to TP adjustments confirmed by DRP on all grounds. There is then the possibility that during the course of any appellate or other future proceeding relating to this case, the instant 3 adjustments on accounts of AMP, Brand Development Fees are deleted/ reduced.
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> In such event of deletion or reduction of the aforesaid 3 adjustments, the margin adjustment (now at Rs.33.91 crores) will stay and stand resurrected and may be computed on the value of the specified international transactions (as directed by the DRP in its instant order referred above). Unless otherwise held by the ITAT or higher legal authority as may be the case. In the event of a partial reduction in the 3 adjustments, the impact on the TP adjustment (margin related adjustment) is to be computed by appropriately using the revised values of the 3 adjustments.
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> The AO passed the Assessment order on 29/102012 making the additions as suggested by the TPO and incorporating the caveat / condition imposed by the TPO.

5.1 From the above it is clear that the DRP has remitted the matter back to the file of TPO to make fresh assessment/determination of Transfer ITA Nos.2344 & 2345/Mds/2012 :- 11 -:

Pricing issues which was executed by the TPO and communicated to AO instead of referring the matter back to the DRP to give appropriate directions to the AO. As per the provisions of Section 144C of IT act the DRP has no power o set side the issue or the remit the matter back to the file of TPO/AO. The ld DRP has to decide the issue and issue directions to the AO. For ready reference we extract the relevant provisions of section 144C of IT act as under:

[Reference to dispute resolution panel.

144C. (1) The Assessing Officer shall, notwithstanding anything to the contrary contained in this Act, in the first instance, forward3a a draft of the proposed order of assessment (hereafter in this section referred to as the draft order) to the eligible assessee if he proposes to make, on or after the 1st day of October, 2009, any variation in the income or loss returned which is prejudicial to the interest of such assessee. (2) On receipt of the draft order, the eligible assessee shall, within thirty days of the receipt by him of the draft order,--

(a) file his acceptance of the variations to the Assessing Officer; or

(b) file his objections, if any, to such variation with,--

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(i)    the Dispute Resolution Panel; and
(ii)   the Assessing Officer.
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(5) The Dispute Resolution Panel shall, in a case where any objection is received under sub-section (2), issue such directions, as it thinks fit, for the guidance of the Assessing Officer to enable him to complete the assessment.

(6) The Dispute Resolution Panel shall issue the directions referred to in sub-section (5), after considering the following, namely:--

(a) draft order;

(b) objections filed by the assessee;

(c) evidence furnished by the assessee;

(d) report, if any, of the Assessing Officer, Valuation Officer or Transfer Pricing Officer or any other authority;

(e) records relating to the draft order;

(f) evidence collected by, or caused to be collected by, it; and

(g) result of any enquiry made by, or caused to be made by, it.

(8) The Dispute Resolution Panel may confirm, reduce or enhance the variations proposed in the draft order so, however, that it shall not set aside any proposed variation or issue any direction under sub-section (5) for further enquiry and passing of the assessment order.

5.2 In the instant case, the DRP has remitted the matter back to the file of TPO to take fresh look of the issues as discussed above. As discussed ITA Nos.2344 & 2345/Mds/2012 :- 12 -:

earlier, the DRP has no power to remit the matter back to the file of the TPO and the DRP alone has to determine the quantum of addition or relief and issue direction to the Assessing Officer. Therefore, we are of the considered opinion that the issue should be remitted back to the file of DRP to consider the submissions made by the eligible assessee and to decide the issue afresh on transpricing adjustments. Accordingly, we set aside the transfer pricing issues and remit the matter back to the file of DRP to decide all the transfer pricing issues afresh on merits. The assessee is free to take up all the transfer pricing issues before the DRP. The assessee's appeal on transfer pricing issues for the A.Y 2005-06 and 2008-09 stands disposed off and allowed for statistical purposes.

6.0 Ground No.9 of the assess's appeal for the A.Y 2005-06 is on obsolete stock:

The AO proposed for addition of Rs.2,21,08,585/- on account of provisions made by the assessee for obsolete stocks. The assessee filed objections before the DRP and the DRP confirmed proposal of the addition made by the AO holding that the liability is contingent in nature. 6.1 Aggrieved by the Order of the AO/ DRP, the assessee is in appeal before us. The Ld.AR of the assessee vehemently argued opposing the addition and also submitted the written submissions as under:

• The Appellant had created a provision for stock obsolescence amounting to INR 22,108,585/- during AY 2005-06.

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• AO disallowed provision for stock obsolescence treating it as a contingent liability as the same was made on a provisional basis and could not be considered as liability accrued during the year. The AO placed reliance on the decision of the Supreme Court in the case of Indian Molasses Co. Ltd. v. CIT [959] 37 ITR 66 (SC).

• The Appellant submits that pursuant to stringent norms prescribed by the Ford Group for inventory monitoring, the Appellant had created the said provision for stock obsolescence on scientific basis, by identifying each part which is obsolete, at both the plant as well as vendor's place.

• In addition, the Appellant submits that the creation of such provision was accepted by the statutory auditors and tax auditors as being in line with Accounting Standard-2 issued by the Institute of Chartered Accountants of India and section 145 of the Act respectively.

• In this regard, reliance has been placed on the following decisions to substantiate the Appellant's claim:

Judicial Precedents		Principle/Ruling
CIT v. Becton Dickinson [2013] (ITA Nos.39-43 of 2012) (Delhi High Court)	•	The Delhi Tribunal had expressed a fin assesse had a foolproof method of iden slow moving or dead stock and had put realizable value for the purpose of va same. Further, the Tribunal had noted

assessee had consistently been following the same method accounting over a period of time and the same was in accordance with the commercially accepted accounting principles of valuation.

• The Delhi High Court upheld the finding and verdict of the Tribunal that the provision for stock obsolescence created by the assessee during the year was an allowable expenditure.

In addition, reliance is also placed on the following decisions:

• CIT v. IBM India Ltd.[2015] 230 taxman 544 (Karnataka High Court) • Hotline Teletube & Components Ltd. v. CIT [2008] 12 DTR 311 (Delhi High Court) The Appellant additionally submits that the facts in the decision relied upon by the AO i.e. Indian Molasses Co. Ltd. v. CIT [1959] 37 ITR 66 (SC) is different from the facts of Ford India's case and consequently cannot be applied in the instant case.

On the other hand the Ld.DR supported the orders of the lower authorities.

6.2 We heard the rival submissions and perused the material placed on record.

As per the provisions of the Income Tax Act, the provisions are not allowable deduction since the expenditure is of contingent nature. The ITA Nos.2344 & 2345/Mds/2012 :- 14 -:

assessee himself has claimed the expenditure under the head Provisions which is the liability contingent in nature. The assessee has not furnished any evidence to prove that the expenditure was ascertained and accrued for the year ending 31.03.2005 for the relevant year. The AO in assessment order given a finding that the assessee has made the provision for obsolete stock on provisional basis. The assessee relied on the decision of the Hon'ble Delhi Court where in Hon'ble High court decided the issue in favour of the assessee. In the cited case Hon'ble High court relied on the reasoning of the tribunal as under:

The assessee is in the business of pharmaceutical products where strict supervision of the quality has to be ensured and these products are mostly surgical needles and medical consumable and if such fast moving items are not sold for a considerably lengthy period. It can be safely said that they have lost their consumable acceptability over a period of time, may be due to advent of new products. After all, as long as the assessee acted in a bona fide manner and has appreciated the business realities in which he is placed, the same should be accepted. The assessee has a foolproof method of identification of slow moving or dead stock and has put the realizable value for the purpose of valuing the same. In fact, the principle of valuation is the cost or the market value whichever is lower. The market value here become obsolete or slow moving it naturally has a lower market value which the assessee has recognized. The assessee has properly identified such stock and has also followed in accordance with commercially accepted accounting principles of valuation. In our view, the CIT(A) was correct in law and on facts to have deleted the addition made by the AO which was based not taking into consideration the hard realities of assessee's business. The addition in our view, is properly deleted and we decline to interfere."

In the instant case the assessee has not established such fool proof method of identification of slow moving and dead stock and ascertained the liability as per the consistent reliable system. Therefore, the facts of the case relied upon by the assessee are not applicable and the addition made by the AO is confirmed and this ground of appeal is dismissed.

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7.0 Ground No.10 of the A.Y.2005-06 is related to the warranty:

During the course of assessment proceedings, the AO found that the assessee has debited a sum of Rs.16,58,15,554/- towards the provisions for warranty expenses. The assessee explained that the cars sold by company carry a warranty in favour of the buyer as per the contractual agreement between the company and the buyer in terms of warranty guide provided to the customer at the time of sale. By virtue of agreement company binds itself to rectify the defects arising out of any mechanical failure, free of any cost to the buyer. The accounting treatment for the provision has been followed by the company consistently over the years. However, the AO was not convinced with the explanation offered by the assessee and also distinguished the decision of Hon'ble Supreme Court in the case of Rotoritc controls India Pvt.. Ltd., 314 ITR 62 (SC) and disallowed the expenditure and added back to the income. The assessee filed objections before the DRP and the DPR confirmed the addition proposed by the AO. Accordingly, the AO made the addition as proposed in the draft Assessment Order. Against the order of AO/DRP, the assessee is on appeal before us.

7.1 The Ld.AR made arguments at length opposing the addition and made written submissions as under:

• The Appellant is engaged in the business of manufacturing and selling cars. It is common knowledge that the cars sold carry a warranty in favour of the buyer as per the contractual agreement between the Appellant and buyer in terms of warranty guide provided to the customer at the time of sale to a minimum period of 1 year and may extend up to 4 years.

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• By virtue of this agreement the Appellant binds itself to rectify the contracted defects arising if any during the contract period, free of any cost to the buyer. • The Appellant submits that the provision has been created on a scientific and systematic basis backed by in-depth and precise analysis and calculations according to the procedures and principles laid down by the policy of the Appellant. The historic trend summary of the provisions created and related payments made have been enclosed in Page 757 of the Supplementary Paper book. • Further reliance is placed on the favourable decision of the Hon'ble Chennai Income-tax Appellate Tribunal in the Appellant's own case for AY 1999-00 and AY 2004-05 (enclosed in case law paperbook) wherein provision for warranty has been finally allowed as a deduction. The Hon'ble Tribunal observed that the issue was covered in favour of the Appellant in view of the Apex Court's ruling in the case of CIT v. Rotork Controls India Limited (2009) 314 ITR 62. • Given the above, it is requested that the provision created towards warranty be considered as a deductible expenditure under the provisions of the Act. • Notwithstanding the above, the following case laws support the Appellant's position:

Judicial precedents	Principle/Ruling
Bharat Earth Movers v. CIT [2000] 245 ITR 428 (SC)	It was held that the provision created by the assess meeting the liability incurred by it under leave enc scheme proportionate to the entitlement earned by th

employees was entitled to deduction out of the gross receipts for the accounting year during which the provision was made for the liability and it will not tantamount to contingent liability on account of reasonable quantification of the same. 7.2 Per contra the Ld.DR relied on the lower authorities orders. 7.3 We heard both the parties and perused the material placed on record.

On similar facts, ITAT Chennai 'D' Bench in ITA No.2976 to 2979/Mds/2014 for the A.Ys 1998-99, 2001-02 to 2004-05 dated 26.06.2015 allowed the appeal of the assessee placing reliance on the decision of Hon'ble Supreme Court in 223 CTR 425.

Respectfully following the aforesaid decision of this Tribunal we allow the assessee's appeal.

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> 8.0 Ground No.11 for the A.Y. 2005-06 is related to the disallowance u/s.35D amount to Rs.10,01,086/- In the draft assessment order, the AO proposed to disallow the expenditure amortized u/s.35D of IT Act. The Ld.DRP agreed with the AO's proposal and issued directions u/s144C of IT act and the AO made the addition.
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> 8.1 During the appeal, the Ld.AR submitted that the assessee is claiming the said expenditure u/s.35D from the AY 1997-98 and the subject AY is 9th year of the Claim and the AO has not disallowed the above expenditure during any of the previous years. In his written submissions the A.R submitted as under:
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> • During the financial year 1995-96, the Appellant had incurred expenditure towards stamp duty, registration charges for increase in authorized capital and other related expenses aggregating to INR 10,010,086.
>
> • The Appellant has been consistently claiming one-tenth of the given preliminary expenses as deduction under section 35D of the Act every year from AY 1997-98 and the subject assessment year is the ninth year of claim.
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> • The AO disallowed the given claim on the premise that the expenditure incurred is not related to the expansion of the industrial undertaking.
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> • The Appellant submits that the AO had erroneously construed that the expenditure had arisen subsequent to commencement of business and that he has failed to appreciate that the same had been incurred at the time when the business was not "set-up". The Appellant had submitted that the AO has wrongly examined the preliminary expenses under section 35D (1)(ii) and not section 35D(1)(i), as is applicable in the instant case.
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> • Additionally, it is submitted that the claim has not been disallowed during any of the previous years.
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> • Given that the expenditure had been incurred before the commencement of business, the Appellant submits that there is no requirement for the expenditure to correlate with expansion of the undertaking to validate deductibility under the Act.

• The breakup of the preliminary expenses incurred by the Appellant during AY 1996-97 has been provided below:

No.	Nature of expenses	Amount
1	Stamp duty for increase in Authorized Capital	3,
2	Registration charges for increase in Authorized Capital	5,
3	Others (eg. Fees for Registration of a Company)	
	Preliminary expenses incurred in AY 1996-97	10,

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8.2 We heard the rival submissions and perused the material placed on record.

The assessee is entitled for amortization of expenses incurred before the commencement of business and after commencement of business for extension or in connection with the setting up of new unit. In this case, the assessee has incurred the expenditure before setting up of the unit as evidenced from the details and nature of expenditure referred above and as stated by the assessee the expenditure was incurred in 1996-97 relevant to the AY 1997-98. The assessee has made the claim from AY 1997-98 onwards and no disallowance was made during any of the previous years. The AO has not brought on record any evidence controvert the submissions made by the assessee. No new fact has been brought on record to disallow the expenditure in the year under consideration to make the disallowance, having allowed in the earlier Assessment years. Therefore, we hold that the assessee is eligible for deduction u/s.35D and accordingly the appeal of the assessee on this issue is allowed.

9.0 The next issue is carry forward and set off of unabsorbed depreciation for the AY 1997-98,1998-99 and 1999-2000. This issues is involved in both the AYs 2005-06 & 2008-09. The AO in the Assessment ITA Nos.2344 & 2345/Mds/2012 :- 19 -:

Order, did not allow the carry forward and set off unabsorbed depreciation losses loss for the AY 1997-98 as per the following reasons:

In the statement of total income filed along with the Return, the assessee claimed the unabsorbed depreciation losses of following years.

- Assessment year 1997-98 : Rs.4,05,34,542
- Assessment year I 998-99 : Rs.3,31 27,564
- Assessment year 1999-00 : Rs.8,27,63,426

As per provisions of sec.32(2) of the Act, as applicable for the above assessment years, unabsorbed depreciation can be carried forward only for a period of subsequent 8 assessment years and can be set off only against business income of subsequent years. Only with effect from asst year 2002-03, sec.32(2) has been amended to the effect that unabsorbed depreciation losses would be merged with subsequent years depreciation and deemed to be part of that allowance. This amendment is applicable only from asst year 2002-03 and for the above years, viz., 1997-98 to 1999-2000, as per provisions of sec.32(2), the unabsorbed depreciation is allowed to be carried forward and set off against business profits of subsequent 8 asst years.

Out of the unabsorbed depreciation of Rs.4,05,34,542/- of A.Y.1997-98, an amount of Rs,1,85,57,771/- is now set off against profits of A.Y.2005-06, as shown above. The balance unabsorbed depreciation of Rs.2,19,76,771/- pertaining to A.Y.1997-98 cannot be carried forward beyond asst year 2005-06 as per the provisions of sec.32(2) of the Act applicable for this year.

Similarly, unabsorbed depreciation of AY.1998-99 (Rs.3,31,27,564) and A.Y.1999-2000 (Rs.8,27,63,426) cannot be carried forward beyond asst years 2006-07 and 2007-08 respectively, as per the provisions of sec.32(2) of the Act applicable for these assessment years.

9.1 During the appeal hearing, the AR of the assessee made the following submissions orally as well as in writing:

The Appellant submits that the AO has erred in restricting the carry forward of unabsorbed depreciation of the earlier years by erroneously interpreting the provisions of law on the aforementioned claim without taking into cognizance that the unabsorbed depreciation of any preceding previous year(s) should be considered as the previous year's depreciation as provided under section 32(2) of the Act (amended by the Finance Act, 2001). The Appellant places reliance on the decision of the jurisdictional Tribunal in the case of KMC Speciality Hospitals India Ltd. [2014] 32 ITR(T) 149 (Chennai Tribunal) wherein it was held that the interregnum restriction of limiting the claim for an eight-year period does not take away the right of an assessee to claim the balance of unabsorbed depreciation, forever. Further, by virtue of the amendment bought out by the Finance Act 2001, the unabsorbed depreciation for the interregnum period (AY 1997-98 to AY 2001-02) would revive back into life and become eligible for carry forward and set off for an indefinite period.

Further, in the case of Best & Crompton Engineering Ltd. [2014] 30 ITR(T) 638 (Chennai Tribunal), the Hon'ble Chennai Tribunal placed reliance on the decision of the Gujarat High Court in the case of General Motors India (P.) Ltd. v. Deputy Commissioner of Income-tax [2012] 354 ITR 244 and held that, the unabsorbed depreciation prior to AY 2002-03 i.e. from AY 1999-2000 to AY 2001-02 would be available for carry forward and set off against income of subsequent years without any time limit in view of the section 32(2) as amended by Finance Act, 2001.

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The observations made by the Gujarat High Court in the case of General Motors India (P.) Ltd (supra) and followed by the Chennai Tribunal in the case of Best & Crompton Engineering Ltd. (supra) are elucidated below:

• Prior to the Finance Act No.2 of 1996, the unabsorbed depreciation for any year was allowed to be carried forward indefinitely and by a deeming fiction became allowance of the immediately succeeding year. The Finance Act No.2 of 1996 restricted the carry forward of unabsorbed depreciation and set-off to a limit of 8 years, from the AY 1997-98. CBDT Circular No.762, dated 18 February 1998, in the form of Explanatory Notes categorically provided, that the unabsorbed depreciation allowance for any previous year to which full effect cannot be given in that previous year shall be carried forward and added to the depreciation allowance of the next year and be deemed to be part thereof. So, the unabsorbed depreciation allowance of AY 1996-97 would be added to the allowance of AY 1997-98 and the limitation of 8 years for the carry-forward and set-off of such unabsorbed depreciation would start from AY 1997-98.

• The provision of section 32(2) was introduced by Finance (No. 2) Act, 1996 and further amended by the Finance Act, 2000. The provision introduced by Finance (No. 2) Act, 1996 was clarified by the Finance Minister to be applicable with prospective effect. This amendment has become applicable from AY 2002-03 and subsequent years meaning that any unabsorbed depreciation available to an assessee on 1st day of April, 2002 (AY 2002-

03) will be dealt with in accordance with the provisions of section 32(2) as amended by Finance Act, 2001 and not by the provisions of section 32(2) as it stood before the said amendment. If the intention of the Legislature had been to allow the unabsorbed depreciation allowance worked out in AY 1997-98 only for eight subsequent AYs even after the amendment of section 32(2) by Finance Act, 2001, it would have incorporated a provision to that effect. However, it does not contain any such provision. Hence, a purposive and harmonious interpretation has to be taken keeping in view the purpose of amendment of section 32(2). While construing taxing statutes, rule of strict interpretation has to be applied, giving fair and reasonable construction to the language of the section without leaning to the side of assessee or the revenue. But if the Legislature fails to express clearly and the assessee becomes entitled for a benefit within the ambit of section by the clear words used in section, the benefit accruing to the assessee cannot be denied.

• However, Circular No.14 of 2001 had clarified that under section 32(2), in computing the profits and gains of business or profession for any previous year, deduction of depreciation under section 32 shall be mandatory. Therefore, the provisions of section 32(2) as amended by Finance Act, 2001 would allow the unabsorbed depreciation allowance available in the AYs 1997-98, 1999-2000, 2000-01 and 2001-02 to be carried forward to the succeeding years, and if any unabsorbed depreciation or part thereof could not be set off till the AY 2002-03 then it would be carried forward till the time it is set off against the profits and gains of subsequent years.

• It is held that any unabsorbed depreciation available to an assessee on 1st day of April, 2002 (A.Y 2002-03) will be dealt with in accordance with the provisions of section 32(2) as amended by Finance Act, 2001. And once the Circular No.14 of 2001 clarified that the restriction of 8 years for carry forward and set off of unabsorbed depreciation had been dispensed with, the unabsorbed depreciation from AY 1997-98 up to the AY 2001-02 got carried forward to the AY 2002-03 and became part thereof, it came to be governed by the provisions of section 32(2) as amended by Finance Act, 2001 and were available for carry forward and set off against the profits and gains of subsequent years, without any limit whatsoever.

The aforesaid principles have been reiterated and relied on by the following judicial precedents --

• CIT v. Gujarat Themis Biosyn Ltd. [2014] 228 taxman 359 (Gujarat High Court) • Arc Fine Chemicals Private Limited v. ACIT [PTA No. 2414/2415/2012] (Mumbai Tribunal) • Confidence Petroleum India Ltd v. OCIT [PTA No. 1937/ 2012] (Mumbai Tribunal) • DCIT v. Bajaj Hindustan Ltd. [2014] 149 ITD 709 (Mumbai Tribunal) • Smith & Nephew Healthcare (P.) Ltd. v. DCIT [2014] 32 ITR(T) 208 (Mumbai Tribunal) • Hindustan Unilever Ltd. v. ACIT [2012] 22 ITR(T) 737 (Mumbai Tribunal) ITA Nos.2344 & 2345/Mds/2012 :- 21 -:

> In addition to the above, the jurisdictional Madras High Court in the case of CIT V. S & S Power Switchgear Ltd. [2009] (218 CTR 701) (Madras) had upheld the principle that that the unabsorbed depreciation allowance of one year shall be added to the depreciation allowance of the next year and will be deemed to be the allowance of that year. Furthermore, the Hon'ble Chennai Tribunal in the case of DCIT V. Tamil Nadu State Transport Corporation (Villupuram) Limited [2012] I.T.A. No. 1713/Mds/2011 had placed reliance on Circular 762 (supra) and the aforesaid ruling and held as under:
>
> "In view of the above circular, and also in view of the decision of the jurisdictional High Court, in the case of CIT v. S & S Power Switchgear Ltd., (218 CTR 701) (Madras) the entire depreciation that was brought forward to the AY 1996-97 and the net unabsorbed depreciation computed for the AY 1996-97 and carried forward to the AY 1997-98 becomes the depreciation allowance of AY 1997-98. The unabsorbed depreciation allowance after set off against the income of the current year, will become the unabsorbed depreciation allowance of AY 1997-98 and the limitation of 8 years, as per the amended provisions of sec.32(2), starts from the AY 1997-98. Therefore, all the depreciation allowances that are brought forward from the earlier

> years and were available during the AY 1997-98 can be carried forward for another period of 8 years i.e., up to AY 2005-06. In any case, with the change in the provisions of section.32(2) w.e.f. 01.04.2002 the unabsorbed depreciation once again was made available to the assesse indefinitely by clubbing with the current depreciation allowance."

In light of the above jurisdictional decisions, the Appellant had submitted that the brought forward unabsorbed depreciation of AY 1997-98, 1998-99 and 1999-2000, to the extent not set-off against the income of AY 2005-06, be allowed to be carried forward to the future years for an indefinite period.

9.2 We heard the rival submissions and perused the material placed on record. The Ld.AR relied on the decision of this Tribunal in of DCIT V. Tamil Nadu State Transport Corporation (Villupuram) Limited [2012] I.T.A. No. 1713/Mds/2011 Circular No.14 of 2001 and jurisdictional High Court of Madras cited supra. This issue is squarely covered by the decision of this Tribunal and the case law relied upon by the assessee cited supra. 9.3 Respectfully following the order of this Tribunal in the cited case we direct the AO to allow the unabsorbed depreciation of AY 1997-98, 1998-99, 1999-2000 to the extent not set off against the income of the AY 2005-06 for future years. The appeals of the assessee on this issue for the AY 2005-06 & 2008-09 are allowed.

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10.0 The next ground for the AY 2008-09 was depreciation on UPS:

> The AO disallowed the depreciation on UPS amounting to Rs.6,47,180/- holding the UPS as general plant and machinery The assessee claimed the depreciation @60% treating the UPS as a part of computer. The Hon'ble ITAT'C' Bench, Chennai in ITA N.01774/Mds/2012 in the case of Sundaram Asset Management Co. Ltd vs DCIT held that UPS is an integral part of computer and eligible for Depreciation @60%. Respectfully following the decision of this tribunal in case cited (Supra) we direct the AO to allow the Depreciation on computer @60%. In the result, the assessee's appeal is allowed.

11.0 The next issue in Ground No.9 for AY 2008-09 is disallowance of Rs.44,11,27,098/- relating to the reversal of the provision for non- deduction of tax at source. The Ld.AR submitted during the hearing that the AO has passed necessary rectification order on 16.10.2014 on application filed by the assessee. Therefore, this ground is dismissed as infructuous.

12.0 Ground No.10 for the AY 2008-09 is credit for tax withheld at source amounting to Rs.74674/- The AO is directed to allow the credit for the tax withheld after making due verification.This ground of appeal is allowed for statistical purposes.

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13.0 Ground No.12 is related to the refund due to the company on withholding tax. The AO allowed the interest on refund due to the Company as per the credit available according to NSDL records but not on the actual TDS receivables claimed by the company. The AO is directed to verify the receivables and allow interest as permitted by the law. This ground of appeal is allowed for statistical purposes. 14.0 In the result, the appeal of the assessee is partly allowed.

Order pronounced in the Open Court on 12th May, 2017, at Chennai.

Sd/-	Sd/-
(. . .)	(" . . $)
(N.R.S. GANESAN)	(D.S.SUNDER SINGH)
/JUDICIAL MEMBER	/ACCOUNTANT MEMBER

/Chennai,
5 /Dated: 12th May, 2017.
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1. -/Appellant	4. 8 /CIT
2. ./ -/Respondent	5. 6 / . /DR
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