Philips Electronics India Ltd., ... vs Assessee on 16 March, 2009

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IN THE INCOME TAX APPELLATE TRIBUNAL, BENCH "B", KOLKATA

  (  ¢)Before      .
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               Shri B.R.Mittal, Judicial Member.
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                       .  .
                          .   ,
              Shri C.D.Rao, Accountant Member
           É   /
ITA No1075/Kol/2009
    ¡    ¢£/Assessment Year : 2003-04

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           (     /¥/APPELLANT )                        -       (ƒ× /¥/RESPONDENT)
       D.C.I.T., Circle-11, Kolkata          Versus- M/sa.Philips Electronics
                                               .    India Ltd., Kolkata
                                                      PAN: AABCP 9487 A

           É   /
ITA No.948/Kol/2009
    ¡    ¢£/Assessment Year : 2003-04

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           (     /¥/APPELLANT )                        -         (ƒ× /¥/RESPONDENT)
M/s.Philips Electronics India Ltd., Kolkata   Versus-      D.C.I.T., Circle-11,
PAN: AABCP 9487 A                              .              Kolkata

      /¥  ¤ '    / For the Appellant:                     Shri B.B.Panigrahi,CIT
 ƒ× /¥  ¤ '    /For the Respondent:                       Shri Bishan Kumar Seal
                                                          & Shri Amitava Sen

                                 “/ORDER
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Per Shri C.D.Rao, AM
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The above cross appeals are filed by the Revenue and the assessee against separate orders dated 16.03.2009 of the CIT(A)-XI, Kolkata pertaining to A.Yr. 2003-04.

2. The first two grounds raised by the Revenue as well as first three grounds raised by the assessee are relating to the transfer pricing adjustments.

3. The brief facts of this issue are that while doing the scrutiny assessment following adjustments have been made by the AO under the following heads :

Sl.No.	Items	Amount of adjustment
1.	Import of monitors	1,56,38,800/-
2.	Export of Finished goods Commercial and CE Industrial)	(CE 88,49,308/-
3.	Export of ETG	6,99,032/-
4.	Payment of I.T.charges	1,09,16,882/-
5.	Re-imbursement of expenses	13,01,000/-
	Total	3,74,05,022/-

3.1. By observing that the assessee has made international transactions with its associated enterprises during the year and with prior approval from CIT u/s 92C the transactions were referred to the Transfer Pricing Officer for determination of Arm's Length Price. The Transfer Pricing Officer has furnished his report which has been discussed with Shri Mondal, ld. AR of the assessee. By virtue of Sub-section (4) of Section 92C the total income will be computed in regard to the computation of Arm's Length Price and the adjustments to be made therein. Thus sum will, however, not qualify for any deduction under Chapter VIA. The report of the T.P.O. is attached to this order vide Annexure-I. 3.2. Aggrieved by this the assessee went in appeal before the ld. CIT(A). 3.3. On appeal the ld. CIT(A) has deleted the additions on account of exports of ETG and payment of IT charges by observing as under :-

> "Export of ETG :The assessed exported finished goods of Rs.79,88,944/- in its ETG Division. The explanation of the assessee as well as the decision of the Transfer Pricing Officer here is on the same lines as in respect of the export of goods of CE division discussed earlier. Here, the contribution margin on exports was found to 27.5% as against overall margin of 33% in this unit. The transfer Pricing Officer applied 33% CM to exports, resulting in adjustment of Rs.6,99,032/-. Considering that the volume of business here is insignificant compared to the overall business of the assessee and differential CM is also not very wide (as distinguished from the differential CM seen in support of goods from CE division), it is held that the adjustment should better be ignored. The purpose of transfer pricing legislation is not to make adjustments on the basis of mathematical formula but to neutralize the effect of shifting of profits from one jurisdiction to another in the course of related party transactions. In this case, it is also seen that the ETG unit at Kolkata was closed by the assessee and the assets thereof were being written off. Hence, the submission that the unsold stock was sold overseas in a situation of distress sale could be accepted without hair-splitting. Considering these facts and circumstances and also the smallness of amount involved, the addition is deleted.
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> Payment of IT Charges : It has been submitted by the assessee that the cost incurred by AE on IT services is allocated to group entities in a uniform manner all over the world. As per the global IT policy of the group, the recovery is effected on the basis of actual user and is quantified on the basis of cost plus 5% markup. The transfer

> pricing analysis done by Emst & Young for Philips International, B.V.Netherlands showed that interquartile range of simple average mark-up on total costs earned by unrelated entities for the period 1997 to 2001 in the European Union, Norway and Switzerland had a median of 5.1%. According to another analysis, such mark-up in Western Europe during the period 2001 to 2003 had a median of 6.1%. The transfer pricing policy adopted by the General Sourcing Unit (GSU) for IT services of Philips International B.V.Netherlands discussed various parameters and laid down that 5% mark-up from the actual cost would be charged as remuneration for the IT services rendered by it to the group companies. It was submitted that such markup, calculated on the basis of the proportional cost determined on the basis of actual user was charged from the assessee as well as the various other companies of Philips group in a transparent manner and based on the publicly disclosed transfer pricing policy discussed above. According to the assessee, this policy is also available on the website of the Philips group. In view of these facts and circumstances, it is held that the price paid by the assessee for IT services utilized by it from the AE was not unreasonable. Consequently, the addition is deleted."

3.4. On the other hand, the ld. CIT(A) confirmed the action on account of three items i.e. import of monitors, export of finished goods and Reimbursement expenses. However, the assessee has come in appeal only on account of import of monitors and export of finished goods. In addition to these two items the assessee has taken ground no.3 by stating that on the facts and circumstances of the case the ld. CIT(A) erred in not granting the benefit of +/- 5% range while computing the arm's length price and consequent adjustment to total income.

3.5. The relevant observations of the ld. CIT(A) on account of import of monitors and export of finished goods are as under :-

> "2.2. Import of Monitors: This argument of the assessee is logically appealing but fails to explain why, if all these products were similar in nature and were complementary to each other, the CM percentage in respect of monitors is only 3.40% while that in respect of other products ranges form 21.35% to 23.56% within the imported segment itself. Even within the locally manufactured segment, the CM percentage in respect of CTV and Audio was 14.95 and 25.94 respectively. As observed by the Assessing Officer, even though monitors and the rest of the products in this division are classified together by the Customs Authorities, they cater to different areas of consumer needs. Even if the assessee's contention that they formed a common group be accepted, it is difficult to accept the exceptionally low CM on monitors as compared to the other products within the same segment. The assessee adopted the average CM percentage on imported items (19.92%) and compared it with the average CM percentage with the locally manufactured items (19.97%) and concluded that its imports were priced at arms length. The Transfer Pricing Officer considered monitors separately and, since monitors were not manufactured locally by the assessee, he identified the CM of unrelated parties for benchmarking CM on monitors in this case. If the products are separately identifiable and their CMs can

separately be worked out, there is no reason why the CM of a particular product should not be benchmarked against that of the product in an unrelated transaction. Hence, the assessee's method of comparing it with the gross CM percentage of its locally manufactured items is not appropriate, particularly considering the fact that monitors do not figure in locally manufactured items and the CM percentage of the monitors within the imported items is exceptionally low compared to the other items within the same segment. 2.3. In his analysis of determining the ALP, the TPO excluded the Government companies and loss making companies. This fact has been contested by the assessee. The TPO was considering the broad spectrum of companies performing distribution function in general. In other words, he was benchmarking the CM on the basis of functional similarity. According to the assessee if the TPO desired to treat monitors as a separate entity, he should also have factored in products similarity, i.e. the CM of companies distributing imported monitors only should have been considered for this exercise. This argument is well taken. But the fact remains that even the assessee has not furnished any such reliable and comparable data in respect of CM of imported monitors in India. There is a prima facie case for transfer pricing adjustment. The benchmarking exercise carried out by the assessee does not appear to be very accurate. But if one goes by assessee's own contention and takes the product within the CE division as similar it is seen that CM percentage on other products ranged from 21.35 to 23.56 as noted above earlier. In view of these facts and circumstances, it is held that the C.M. of 14.04% adopted by the TPO cannot be disturbed. Consequently, the addition made by the Assessing Officer pursuant to the transfer pricing adjustment in the cost of imported monitors is confirmed.

3.3. Export of finished goods : The assessee has not substantiated, with relevant documents, its contention that the stock in question was lying for lack of demand. It is true that the AE was not a retail distributor nor was it the end consumer. It was the original manufacturer/supplier. Hence, all other facts remaining the same, the assessee might be required to share a part of its profit with the AE and, to that extent, some reduction in price may be justified. But, on the other hand, there is also a possibility that the price of these products in the importing country was substantially higher than the price in India and that the AE was in a position to earn its normal profit even after the assessee had sold the products to it after charging its normal profit. Such analysis is not available on record. In this situation, it is felt that there is no justification to interfere with the finding of the TPO/Assessing Officer. Consequently, the addition is confirmed."

4. At the time of hearing before us, the ld. Counsel appearing on behalf of the assessee has supported the orders of the ld. CIT(A) as far as deletion of export of ETG and payment of IT charges but however, the ld. Counsel for the assessee after discussing various criteria for computation of arms length price in respect of transactions with associated enterprises, he finally concluded that the Transfer Pricing Officer has not given sufficient opportunity to explain the case of the assessee.

5. The ld. DR appearing on behalf of the Revenue contended that the action of the ld. CIT(A) in deleting of the two items i.e. import of ETG and payment of IT charges is not based on sound reasoning. Therefore he requested to uphold the action of the AO on these two issues.

6. After hearing the rival submissions and on careful consideration of the materials available on record we have observed that the Transfer Pricing Officer has taken sufficient time while preparing arms length price in respect of the enterprise transaction. Since the main contention of the assessee is that the Transfer Pricing Officer has not given sufficient opportunity we are of the considered view that the matter may be set aside to the file of the AO with the direction to obtain fresh report from the T.P.O. and the T.P.O. is directed to recomputed the transfer price after giving reasonable opportunity of being heard to the assessee.

7. Regarding the Revenue's appeal we find that the reasoning given by the ld. CIT(A) for deletion is not appropriate and the ld. CIT(A) has accepted the contention of the assessee which are general in nature and not discussing the facts of the case. Since we have already set aside the issues involved in assessee's appeal to the file of the AO for taking fresh report from the T.P.O. the issue deleted by the ld. CIT(A) is also being set aside to the AO with the similar observations.

8. In the result the first two grounds of assessee as well as Revenue's are allowed for statistical purposes.

9. As regarding ground No.3 raised by the assessee the specific observations of the ld. CIT(A) are as under :-

> "Another ground (Ground NO.9) is that, while making transfer pricing adjustments, the Transfer Pricing Officer did not give the benefit of plus minus 5% range as provided in Section 92C(2)of the Income Tax Act. According to the said provision, where more than one price is determined by the most appropriate method, the ALP would be arithmetical mean of such price or, at the option of the assessee, the price which may vary from the arithmetical mean by amount not exceeding 5% of such arithmetical mean. It is not that, even when the most appropriate method yields only one price, the benefit of 5% variation has to be allowed to the assessee. In this case, according to the most appropriate method adopted by the Transfer Pricing Officer, the price determined was one, and not more than one in each case. Hence, there was no occasion to allow 5% variation therein. Hence, this ground is rejected."

10. At the time of hearing before us the ld. Counsel appearing on behalf of the assessee by narrating the provisions of section 92C(2) of the IT Act and by placing reliance on the following case laws :

> a) Development Consultants Pvt.Ltd. vs DCIT, Circle-11, Kolkata (2008) 115 TTJ 577
>
> b) Tata Tea Limited vs ACIT, Circle-4, Kolkata
>
> c) Sony India (P) Ltd vs DCIT (2008) 114 ITD 448 (Delhi)

d) Skoda Auto India Pvt Ltd. Vs ACIT, Circle-1, Aurangabad (ITAT,Pune)122 TTJ 699.

He contended that AO should have given plus or minus 5% adjustment as per section 92C(2) of the IT Act.

11. On the other hand, the ld. DR has submitted that since in this case the provision of Section 92C(2) of the IT Act will not be applicable since the TPO has adopted the only one method i.e. most appropriate method and the provision of Section 92C(2) of the IT Act is applicable when there are more than one price adopted by the TPO. In view of this no adjustment as required u/s 92C(2) of the IT Act is required. Therefore he requested to upheld the action of the ld. CIT(A).

12. After hearing the rival submissions and on careful consideration of the material available on record including the case laws relied upon by the assessee we are of the considered opinion that when only one price has been determined under (most appropriate method) for evaluating arms length price, the question of applicability of proviso 2 of section 92C(2) does not arise. Therefore assessee, was not entitled to the concession of plus or minus 5% as prescribed in the said provision.

13. In the result ground no.3 of the assessee is dismissed.

14. The last ground raised by the Revenue in this appeal is relating to deletion of motor car expenses and payments for acquisition of motor cars.

15. The relevant facts of this issue are that the AO while doing the scrutiny assessment has disallowed an amount of Rs.70,00,000/- by observing that the assessee has claimed deduction in computation of total income the payment of lease rental on cars taken on financial lease amounting to Rs.70,00,000/-. The assessee has submitted the copies of the lease agreement with Leaseplan India Ltd. The features of the agreement such as warranties, manufacturers warranties, vehicle in transit, delivery and disbursement, registration of vehicle, insurance and repairs, loss and damage the AO is of the view that from the foregoing clauses of the agreements it is clear that the vehicles were chosen by the assessee taken delivery by or at the option of the assessee, registered in the name of the assessee, insured in the name of the assessee and by the assessee, and also repaired at the cost of the assessee. By taking into consideration of these facts he concluded that for all practical purposes the assessee is the owner of the cars and the instalments for purchase is paid to so-called Leaseplan India Ltd. Although the assessee called the term lease rental it is nothing but the instalments paid for the purchase of motor cars. As these are paid for the purchase of the capital asset, the instalments are not allowed as revenue expenditure.

15.1. On appeal the ld.CIT(A) has deleted the same by observing as under :-

> "9.4. The Assessing Officer analysed the lease agreement with Leaseplan India Ltd. And came to the conclusion that the assesee was the real owner of the cars and Leaseplan India Ltd was just a financier and that the lease agreement was in substance of financing arrangement. Having said that, he hurriedly disallowed the

> payment of Rs.70 lakhs by the assessee to Leaseplan India Ltd as the same was not revenue expenditure according to him. He failed to take his own finding to the logical conclusion because, if the assessee is the real owners of the cars, depreciation has to be allowed to it. In addition, the interest component of payment to Leaseplan India Ltd would also have to be allowed. Hence, the decision of the officer, as it is, can not be sustained. If the decision of the Assessing Officer is taken to its logical conclusion, there will be another related consequence to that. As per certificate submitted by the assessee from Leaseplan India Ltd the latter is claiming and getting depreciation in respect of the same vehicles. It is obvious that two persons cannot be granted depreciation allowance simultaneously in respect of the same asset at the same time. Hence, if the logic of the Assessing Officer is taken forward it will lead to consequences affecting the assessment of Leaseplan India Ltd as well. In the considered opinion of the undersigned, the facts on record are not sufficient to justify an adverse decision of such far-reaching consequences. Considering the totality of the facts and circumstances, as they appear form the material available on record, the addition is deleted."

15.2. Aggrieved by this the revenue is in appeal before us.

15. In this case the Ld DR appearing on behalf of the Revenue submitted that the observations of the AO were correct as the vehicles were used wholly and exclusively by the appellant and therefore the ownership also was lying with the appellant. That the lessor was claiming depreciation cannot be the ultimate test for ownership of the lessor. On the other hand the CIT(A) wrongly held that the ownership did not pass on to the lessee and thus the financial charges or lease rent should be allowed. This is wrongly found as the lessor might have sold the assets to the lessee or the user of the vehicle.

16. On the other hand the ld. AR appearing on behalf of the assessee submitted that the AO had disallowed the lease rent paid by the appellant on the ground that the ownership of the vehicles lie with the appellant and explained certain clauses of the agreement related to warranties, manufacturers warranties, vehicle in transit, delivery and disbursement, registration of vehicle, insurance and repairs, loss and damage. The Ld.AO has erred in holding that the lease rent paid was for purchase of capital asset.

The AO had ignored the clauses/sub clauses related to ownership of the vehicles. The Ld. AO had not examined the clauses named 'Title, Identification, Ownership of the Vehicle', 'Surrender', 'Event of default' and 'Remedies' clauses. (Please refer the attached lease agreement, page 141 to 146 of the paper book). The clause 'Title, Identification, Ownership of the Vehicle' deals with the right and title of the vehicle. (Page 142 of paper book) This clause clearly explains that the vehicle under the lease shall be the sole and exclusive property of the lessor and the lessee shall have no right therein except the right to use the same in accordance with the leasing document and that the vehicle shall at all times remain the property of the lessor. The lessee also undertakes not to sell, assign, sublet and hypothecate the vehicle.

16.1. The clause 'Surrender' deals with delivery of the vehicle to the lessor on the expiry or earlier termination of the lease. (Page 144 of paper book) -In practice all the vehicles are returned to the lessor, who has the discretion to sell to a new party. Also once the vehicle is returned the Form 35 is signed and accordingly a No - objection is given by Lessor that they have no objection is deleting their name and transfering the name to a new owner along with insurance cover. (Page 148 of papaer book).At the time of termination of agreement, the Lessor issues Form 35 categorically declaring that 'agreement of Hire Purchase/Lease/Hypothecation entered into between us has been terminated. We, therefore, request that the note endorsed in the certificate of Registration Vehicle No.... in respect of the said agreement between us, be cancelled'. (refer pg 149 of the paper book).The word terminated indicates that the Lessee has discharged all the obligations mentioned in Lease agreement which includes return of car by the appellant and payment of all the dues. Further, the Lessor issues NOC in favour of RTO agreeing for removal of their name in the Registration Certificate and transfer of same in the name of new owner.

16.2. In the 'Event of Default' in respect of lease rental by lessee, the main 'Remedies' lies with the lessor is to take the leased asset back from the lessee. It clearly indicates that the ownership of the asset is with lessor only. (Page 144 - 145 of paper book) The above clauses clearly define that ownership of the vehicle lies with the lessor only and lessee's right is limited to the use of the vehicle. It may also be noted that in leasing transactions, the lessor being the owner of the asset, always claims the depreciation under the Income Tax Act. In the case of appellant also, the lessor had claimed the depreciation under the Income Tax Act. Further a confirmation from the lessor, stating that it has claimed the depreciation in the relevant assessment year is also attached in page 147 of the paper book. This confirmation establishes beyond doubt that the appellant is not the owner of the asset, and it is entitled for the deduction of lease rental. Further at the end of the lease period, Form 35 i.e. No objection in transfer of ownership is also given by the lessor (Page 148-149 of paper book) 16.3. In this connection was relied on the Rajasthan High court in the case of Rajshree Roadways vs. Union of India, 263 ITR 206 (2003) and Court after examining the ownership issue has held that lessee would be entitled to the deduction of rent paid by him and the benefit of the depreciation shall be available to the owner of the asset.

16.4. Under the Income Tax Act, an appellant is eligible to claim depreciation on any asset u/s 32 only if such assets is owned by him and is used for the purpose of his business. The CBDT's views on the treatment of finance lease for the purpose of determining ownership and thereby depreciation allowance is however not aligned to the accountant's perspective of a finance lease. The principles governing eligibility of lessor to claim tax deprecation under the lease arrangement is enunciated by administrative guidelines issued by the CBDT in circulars 9/1943 and 2/2001. The circulars do not distinguish between the two kinds of lease arrangement and provides that in a lease other than a hire purchase, the lessor is eligible to claim depreciation provided the test of ownership and use of asset are satisfied. The principles laid down in Circular No. 9 dated 23-03-1943 provides that where the terms of agreements provides that equipment shall eventually become the property of the hirer or confer on the hirer an option to purchase the equipment, the transaction should be regarded as one of hire-purchase and the lessee will be entitled to depreciation in that case. Circular 2/2001 dated 09-02-2001 has clarified that AS-19 which requires capitalization of the asset by the lessees in financial lease transaction, by itself, will have no implication on the allowance of depreciation on assets under the provisions of the Income-tax Act. The ownership of the asset is required to be determined by the terms of contract between the lessor and the lessee. The A/R submitted that in the instant case it is the lessor who had remained the owner and even at the end the vehicles are returned to him by the appellant company.

16.5. On the basis of above, the A/R submitted before the Bench that the CIT(A) has rightly directed the AO in deleting the disallowance and allowing the lease rental of Rs. 7,000,000/- and the same may be upheld. He further pointed out that this is the only year in which such issue arose as in the subsequent years as late as AY 2006-07 & AY 2007-08 the issue was consistently allowed by the AO.

17. After hearing the rival submissions and on perusal of the page numbers of the paper book referred by assessee as well as AO we are of the view that the action of the Assessing Officer is quite justifiable in the facts and circumstances of the case when compared to that of ld. CIT(A). Therefore, we set aside the orders of ld.CIT(A) on this issue and restore that of AO.

18. In the result ground no.3 of the revenue's appeal is allowed.

19. As regarding ground no.4 taken by the assessee is in respect of disallowance of provision for replacement guarantee. The relevant facts are that while doing the scrutiny assessment the AO has disallowed the provision of replacement of guarantee charges amounting to Rs.10,24,78,000/- by observing that as this is mere provision it is not allowed as deduction. However, the AO has allowed the actual payment in this year amounting to Rs.10,14,41,000/-.

19.1. On appeal the ld. CIT(A) has confirmed the action of the AO by observing as under :-

> "10.11 Considering the facts and circumstances of the case discussed above it is held that warranty obligations which would arise in future is not an expenditure and amount set aside for meeting such future obligation cannot be allowed as a deduction in the current year. This decision is based on the decision of the Hon.Supreme Court in the case of Indian Molasses Company (37 ITR 78ITR 475) referred to above and with due regard to the other view sectioned by other decisions of courts/tribunals. It may be reiterated that the facts of this case are peculiar in so far as the assessee has accepted deduction on the basis of actual expenditure in the past and, in one of such instances (AY 1997-98), the actual expenditure was more than the provision made in that year, as a result of which it got higher deduction than was claimed by it in the return of income. Hence, this decision is based more on the facts of the case; the legal aspect is adjunct to the factual one. With these observations, the addition is confirmed."

19.2. Aggrieved by this the assessee is in appeal before us.

20. At the time of hearing before us the ld. Counsel appearing on behalf of assessee by placing reliance on the paper book wherein assessee has given a chart containing the opening balance, amount charged in the P/L account by creating the provision and actual payments made during the

assessment years and the closing balance since assessment years 1995-96 to 2004-05, based on the contents on the actual expenditure incurred and the provision created he substantiated that the provisions are scientifically computed to cover against the cost of free replacement during the warranty period. Therefore, he finally contended that after the decision of Hon'ble Apex Court in the case or Rotork Controls (India) Pvt. Limited vs CIT 180 Taxman 422 (SC) wherein it is held that provision for warranty is allowable deduction provided it is ascertained on a scientific basis and with reasonable accuracy. Therefore he requested to allow the claim of assessee.

21. On the other hand, the ld. DR appearing on behalf of the Revenue contended that in this case assessee has not proved how the provision has been calculated and whether this is scientifically proved or not. However, AO has already allowed the actual amount of expenditure incurred against the warranty. Therefore, no provision is to be allowed.

22. After hearing the rival submissions and on careful perusal of materials available on record, keeping in view of the statement filed by assessee and on careful perusal of the provisions created as well as the expenditure incurred on account of warranty, we are of the view that the provisions are based on the previous years data and based on the sales and AO himself has allowed the provisions made by assessee in Assessement year 2004-05 while doing the assessment u/s 143 itself we are of the view that assessee is entitled to deduction of provisions in view of the decision of the Hon'ble Supreme Court in the case of Rotork Controls (India) Pvt. Ltd. vs CIT (supra). We direct AO to allow the provision on account of replacement of guarantee for assessment year involved in this appeal.

23. In the result ground no.4 of assessee's appeal is allowed.

24. As regarding the last ground raised by the assessee which relates to the disallowance of advances written off.

25. The brief facts of this issue are that while doing the scrutiny assessment, the AO has disallowed an amount of Rs.6,30,00,000/- by observing as under :-

> "14. The assessee claimed bad debts written off amounting to Rs.6,30,00,000/- . The assessee was asked to furnish the details of the assessment years in which the amount was included in sales. As per provisions of Section 36(2) in the case of an assessee which does not run a banking or money lending business, the amount claimed to be the bad debt, must have been credited into sales. The assessee could not furnish the details of units to which the debts relate. Moreover, the assessee sells the finished products to the distributors/dealers who has no scope for not making the payments and run away without making the payment. Hence it is not proved that the receivables actually became bad. As the most vital information has not been filed, the amounts claimed to have been written off failed to qualify to be written off. As such the amounts were not allowed to be written off."

25.1. On appeal the ld. CIT(A) has confirmed the disallowance to the extent of Rs.52,67,000/- and deleted the balance by observing as under :-

> "11.3. No doubt, trade debts are also a Balance sheet item. But, there is a specific provision, viz.(Sec.36(1)(vii)r.w.s. 36(2) of I.T.Act, for allowing deduction when the same are written off. In such a situation, it ahs to be examined whether the deduction can be allowed under any other section. The assessee has claimed deduction u/s 28. But that section deals with the items of income falling under the head 'Profits and gains of business or profession". It does not deal with deductions. The section under which such a deduction could be considered is Section 37 of the Income-tax Act, according to which, any expenditure laid out or expended wholly and exclusively for the purpose of the business is allowable as a deduction. But the Section applies only to expenditure "not being in the nature of capital expenditure". As mentioned above, trade advances cannot be called 'revenue expenditure' and, hence, allowance of the same is specifically excluded from the purview of Section 37 of the Income-tax Act also. As mentioned by the Hon'ble Supreme Court in the case of Badridas Daga referred to above, a loss which arises directly from the carrying on the business and is incidental to it should be allowed as deduction "provided that there is no provision against it, expressed or implied, in the Act." As mentioned above, the section under which the deduction could be considered contains an express provision prohibiting deduction of capital expenditure. Hence, it is held that the deduction in respect of the amount of Rs.52,67,000/- representing advances written off, cannot be allowed as a deduction. Consequently the addition is reduced to Rs.52,67,000/-."

25.2. Further aggrieved by this the assessee is in appeal before us.

26. At the time of hearing against the above allegations the ld. AR appearing on behalf of the assessee submitted that the company is mainly engaged in the manufacture and sale of durable consumer electronics goods like television sets, audio sets, domestic appliances etc. Each such product is divided in various divisions (9 in number) namely CE, Light, DAP, Projects, CSI, Mso, ETG, WHPD and S&I. Although the appellant is one and only Phillips India Limited, the operations and achievement of each and every divisions can be captured separately which helps the company to keep a strong MIS. Thus division wise sales and expenses are captured. In the current year the management of the division DAP, Projects & S&I decided to write-off an aggregate sum of Rs. 52.67 lakhs given to various parties for supply of materials and services in the general course of business. However it was found that some of the balance lying as advances given to few parties / suppliers given during the course of the business for purchase of raw materials, charges and other business expenditure, which the appellant would purchase/ obtain from various parties were still outstanding and recoverable. These balances were written off after due negotiation with the parties and only when the parties denied settling the outstanding balances. These are merely trade advances and the write of the same tantamount to trading loss. The details were submitted in pages 190 - 191 of the paper book. The said advances having been given by the appellant to various suppliers / processors in the normal course of its business for acquiring various raw materials and other services, the write off of the same as irrecoverable, is allowable as a normal trading loss while computing the income chargeable under the head "Profits and gains of business or profession", notwithstanding the fact that there is no specific provision for the allowability of the same, contained in Chapter IV-D of the Act, dealing with the computation of income chargeable under the head "Profits and gains of

business or profession". In this connection reliance was placed in the Hon'ble Supreme Court in the case of CIT vs Mysore Sugar Company Limited - 46 ITR 649 (SC) and that delivered by the Hon'ble Madras High Court in the case of Devi Films Private Limited vs CIT - 75 ITR 301, 304 (Mad). It has been held in both the said decisions that that even though the claim for deduction of an amount of advance written off, where such advance had given by an appellant in the normal course and for the purpose of its business, other than on capital account, did not squarely fall under section 10(2)(xi) of the Indian Income Tax Act, 1922 [corresponding to section 36(1)(vii) of the Act of 1961] or for that matter any of the enumerated classes of allowances, the said amount would nonetheless be allowed as deduction while computing the business profits.

26.1. The AR further submitted that it is not the case of the appellant that the sums written off amounting to Rs.52.67 lakhs are to be allowed as deductions under section 36(1)(vii) read with section 36(2) of the Act. Undisputedly, one of the conditions precedent for the allowability of deduction under section 36(1)(vii) of the Act, read with section 36(2) of the Act, with respect to bad debt written off, is that the debt in question must have been previously assessed to tax or the same must have been advanced by an appellant in the course of its usual money lending business. The aforesaid conditions are admittedly not satisfied in the instant case of the appellant. There is no dispute regarding the fact that the said advances given by the appellant to various suppliers for the purchase of raw materials, and services, was incidental to the business of the appellant and therefore the write off such advances is per se allowable as a normal trading loss while computing the income chargeable under the head "Profits and gains of business or profession" in the hands of the appellant.

26.2. In this connection attention was also invited to the principle laid down by the Hon'ble Supreme Court in the case of CIT vs Abdullabhai Abdulkadar reported in 41 ITR 545, wherein it was held that "in order a loss might be deductible it must be a loss in the business of the appellant and not a payment relating to the business of somebody else which under the provision of the Act was deemed to be and become the liability of the appellant. Loss was allowable if it 'sprang directly from and was incidental to' the business of the appellant' ". Therefore a debt was allowable only when it was a debt and arose out of and as an incident of trade.

26.3. The AR stated that the ratio of the said decisions of the Hon'ble Supreme Court is squarely applicable in the instant case of appellant. The impugned advance given by appellant in favour of various parties was for the payment of raw materials and other business expenditure, which the appellant would purchase/ obtain from various parties. The advances given in normal course of business by the appellant was not in the nature of an investment. As the Hon'ble Supreme Court had held in the decision referred to above, it did not matter as to whether or not, the item for which the advance was given was already in existence, having been manufactured, at the time of giving the advance. The said trade advance, being not in the nature of an investment made for smooth operation of the business, is to be allowed as deduction if written off in the books of account as irrecoverable. Incidentally the Hon'ble Kolkata Tribunal while deciding the similar issue in the case of ITC Limited in the assessment year 1991-92 had considered the principles laid down by the Hon'ble Supreme Court discussed above, and thereafter allowed the claim for such write-off of advance. [ITA No 157/Kol/96 DCIT vs. ITC Ltd dated 30th April 2001]. Since such advances are given in the course of the business, it is incidental to the business and its write off may be allowed as a trading loss.

26.4. Further as per the A/R the findings of the CIT(A) is absolutely baseless that such an amount is capital in nature. He submitted that the CIT(A) has merely made a presumption that an advance with respect to normal business is in the nature of capital. In view of the above submissions he requested the Bench to delete the disallowance.

27. The ld.DR on behalf of the Revenue objected to the submissions and held that the expenses were never offered to tax earlier and hence cannot be allowed. However if such advances are properly made against revenue items it cannot be termed as capital receipts. The Ld DR submitted that he relied on the decision of the CIT(A) who had categorically held that it was not for trade. The appellant could not also submit any documents which could prove that such advances were from transaction of trading items and the same can only be restored to the file of the AO if such documents are submitted. Otherwise, the additions confirmed by the CIT(A) may be upheld.

28. After hearing the rival submissions and keeping in view of the arguments made by the ld. Counsel on behalf of assessee, we are of the view that these submissions require fresh verification. Therefore, in the interest of justice we consider it fit to restore this issue to the file of AO for fresh verification and decide the same as per law after giving a reasonable opportunity of being heard to assessee. The assessee is also at liberty to file the additional evidences in support of his submissions.

29. In the result ground no.5 of the assessee's appeal is allowed for statistical purposes.

30. In the result the appeals of revenue as well as assessee are allowed in part for statistical purposes.

Order pronounced in the court on 11.10.2011.

Sd/-

Sd/-

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      B.R.Mittal, Judicial Member                   C.D.Rao, Accountant Member.

      (     )
            )Date: 11.10.2011.
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        Order pronounced by
   Sd/-                    Sd/-
   (JM)                   (AM)
   (NVK)                 (CDR)

R.G.(.P.S.)

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      Copy of the order forwarded to:
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1. M/s. Philips Electronics India Ltd., 7, Justice Chandra Madhab Road, Kolkata-700020.

2 The D.C.I.T., Circle-11, Kolkata.

3. The CIT, 4. The CIT(A)-XI, Kolkata

5. DR, Kolkata Benches, Kolkata × « ƒ /True Copy, “ ‹ / By order, Deputy /Asst. Registrar, ITAT, Kolkata Benches