

(2011) 11 KAR CK 0133

In the Karnataka High Court

Case No : IT Appeal No"s. 2972 to 2974 of 2005

Commissioner of Income Tax and Another

APPELLANT

Vs

Infosys Technologies Ltd.

RESPONDENT

Date of Decision : 04-11-2011

Acts Referred:

Income Tax Act, 1961 — Section 37, 37 (1), 80 HHE

Citation : (2012) 246 CTR 371 : (2012) 349 ITR 588 : (2012) 205 TAXMAN 389

Hon'ble Judges : V.G. Sabhahit, J;Ravi Malimath, J

Bench : Division Bench

Advocate : E. Sanmathi Indrakumar, for the Appellant; Arvind Datar, for the Respondent

Final Decision : Allowed

Judgement

V.G. Sabhahit, J.—These appeals are filed by the Revenue being aggrieved by the order passed by the income tax Appellate Tribunal, Bangalore Bench TV (hereinafter referred to as the Tribunal) in ITA Nos. 794/Bang/1998 (asst. yr. 1994-95), 50/Bang/2001 (asst. yr. 1996-97), 793/Bang/1998 (asst. yr. 1993-94) dt. 31st March, 2005 wherein the appeals filed by the assessee had been allowed. Since all these appeals arise out of the common order passed by the Tribunal, appellate authority and the AO, the facts pertaining to ITA No. 2973 of 2005 are narrated as follows :

2. The assessee-respondent is carrying on the business of development of software and sale of software packages. In respect of asst. yr. 1996-97, the assessee filed return of income on 29th Nov., 1996 declaring an income of Rs. 6,90,06,915. The AO took up the matter for scrutiny assessment and found that for the purpose of computation of total turnover and export turnover, the assessee had failed to take into consideration the expenditure incurred in foreign currency when computing deduction under s. 80HHE of the IT Act, 1961 (hereinafter called the Act"). The AO has also rejected the claim of the assessee that the expenditure had been incurred for the purpose of marketing only and,

therefore the same cannot be deducted before granting deduction under s. 80HHE of the Act. Further, the assessee had taken the premises on lease for a period of six years and he spent a sum of Rs. 15,89,613 for renovation of the building. "The AO held that the extensive repair works done to the building amounts to capital expenditure and consequently, depreciation at the rate applicable to building was allowed and the claim that expense should be treated as a revenue expense was disallowed. The assessee had contributed a sum of Rs. 6.93 lakhs to the Traffic Police at Bangalore to regulate traffic on Hosur Road and the same was claimed as an expenditure under s. 37 of the Act. The AO held that it is the duty of the Traffic Police to regulate the traffic and therefore, contribution made for regulating traffic cannot be treated as a revenue expenditure under s. 37 of the Act and accordingly passed an order of assessment dt. 26th March, 1999. Being aggrieved by the said order of the AO, the appeal was filed before the appellate authority. The appellate authority was of the view that the expenditure incurred in foreign currency has to be excluded while computing the export turnover and total turnover before granting deduction under s. 80HHE of the Act. The appellate authority further held that for the purpose of computation, the method which should be adopted was dealt with and consequently the AO was directed to rework the deduction in accordance with the directions issued. The appellate authority further held that the expenses incurred amounting to Rs. 15,89,613 under the head "Building maintenance expenditure" towards brick work, cement, plastering, painting walls, ceiling and providing and laying ceramic tiles and other works was extensive repairs undertaken by the assessee, which would constitute capital expenditure and affirmed the finding of the AO following the judgment of the apex Court in Ballimal Naval Kishore and Another Vs. Commissioner of Income Tax, So far as expenditure of Rs. 6.93 lakhs given to the traffic police Bangalore to regulate traffic on Hosur Road is concerned, the appellate authority held that the same cannot be treated as expenditure under s. 37(1) of the Act. Consequently, the appellate authority rejected the appeal by order dt. 15th Nov., 2000. Being aggrieved by the said order, the assessee preferred the appeal before the Tribunal and the Tribunal allowed the appeal and held that the expenditure incurred towards repairs was revenue expenditure, the contribution made to Bangalore Traffic Police to regulate traffic at Hosur Road, in a sum of Rs. 6.93 lakhs was due to business compulsions and therefore was entitled to deduction under s. 37 of the Act. The Tribunal further held that foreign exchange expenditure need not be included while computing the total turnover. Being aggrieved by the said order, the Revenue has preferred IT Appeal No. 2973 of 2005.

3. The other appeals IT Appeal Nos. 2972 of 2005 and 2974 of 2005 are filed by the Revenue being aggrieved by the common order dt. 31st March, 2005 passed by the Tribunal which is impugned in IT Appeal No. 2973 of 2005.

4. IT Appeal No. 2973 of 2005 has been admitted on 8th June, 2006 for consideration of the following substantial questions of law :

(1) Whether the Tribunal was correct in holding that s. 80HHE of the Act deduction should be allowed to the assessee without excluding the foreign exchange expenditure incurred by the assessee during the current assessment year ?

(2) Whether the Tribunal was correct in holding that the expenses of Rs. 15,89,613 incurred by the assessee towards brick works, cement, plastering, painting walls, ceiling and providing and laying ceramic tiles, providing M.S. grill, internal sanitary fixtures, sewerage works, supply and fixing of water supply pipes on the leased premises would not amount to major repairs as held by the apex Court in Ballimal Naval Kishore and Another Vs. Commissioner of Income Tax,

(3) Whether the Tribunal was correct in holding that the expenses incurred for repairs and maintenance of leased premises for a period of six years should be treated as an allowable revenue expenditure under s. 30(a) of the Act, without taking into consideration the Explanation which omitted capital expenditure from the purview of s. 30(a) of the Act and the Explanation being only explanatory was always retrospective ?

(4) Whether the Tribunal was correct in holding that the contributions made to Traffic Police, Bangalore to regulate the traffic on Hosur Road, of a sum of Rs. 6,93 lakhs was out of business compulsions and commercial expediency and therefore allowable under s. 37 of the Act ?

(5) Whether the Tribunal was correct in allowing deduction in respect of payments made to police for maintaining traffic without taking into consideration and appreciating that the police were public servants discharging public duty being State Government servants and any payment received to discharge such a public duty is prohibited under law and which is also an offence as per the Indian Penal Code and the Prevention of Corruption Act and therefore, cannot be allowed as a deduction as per Explanation to s. 37 of the Act ?"

5. IT Appeal No. 2972 of 2005 has been admitted on 26th June, 2006 for consideration of the following substantial question of law :

Whether the Tribunal was correct in holding that s. 80HHE of the Act deduction should be allowed to the assessee without excluding the foreign exchange expenditure incurred by the assessee during the current assessment year ?

6. IT Appeal No. 2974 of 2005 has been admitted on 19th June, 2006 for consideration of the following substantial question of law :

Whether the Tribunal was correct in holding that s. 80HHE of the Act deduction should be allowed to the assessee without excluding the foreign exchange expenditure incurred by the assessee during the current assessment year ?

7. We have heard the learned counsel appearing for the appellants and learned counsel appearing for the respondent.

Substantial question of law regarding deduction claimed under s. 80HHE of the Act

8. Sec. 80HHE of the Act provides for deduction in respect of profits from export of computer software. Sec. 80HHC(1) [sic-s. 80HHE(1)] deals with eligibility and s. 80HHC(3) [sic-s. 80HHE(3)] is concerned with computation of quantum of deduction and to claim the deduction under s. 80HHC [sic-s. 80HHE] of the Act two conditions are required to be satisfied (1) the assessee must be in the business of export and (2) sale proceeds of such export receivable in India is in convertible foreign exchange. Sec. 80HHC [sic-Sec. 80HHE] provides for tax incentives if the abovesaid two conditions are satisfied. It is not in dispute that the assessee is engaged in the business of production and export of software from India to foreign countries. It is well settled that to arrive at the deduction, formula to be adopted is :

Profits of the business x export turnover - Total turnover

It is well settled that expenses incurred in foreign exchange to provide technical services outside India cannot be included for the export turnover. According to the contention of the assessee, assessee is not at all involved in providing technical services outside India, it is only producing and exporting software. It is the contention of the assessee that the software is developed at various stages and in some cases, it is also necessary to develop the software ultimately at the site and therefore, amount that is spent in foreign exchange is not towards technical services rendered but it is in connection with export of software. On the other hand, it is the contention of the Department that the amount received as per the certificate issued by the chartered accountant as required under s. 80HHE(4) of the Act would clearly show that the amount that is received is towards providing technical services outside India, in connection with production and development of software and not in connection with export of software or its transmission to its place in India. The AO and the appellate authority have held that amount spent in foreign exchange is towards consulting services outside India and therefore cannot be included in the export turnover to arrive at the deduction under s. 80HHE of the Act. It is clear from the information that is published by the assessee as required under the provisions of the Companies Act, 1956 following information regarding total turnover and expenditure in foreign exchange has been furnished :

Asst. yrs.

Total turnover

Expenditure in foreign currency other than on marketing offices

1993-94

14,52,41,229

2,24,45,978

1994-95

30,08,47,456

7,43,70,642

1995-96

57,70,42,862

10,56,81,309

1996-97

93,41,33,705

15,72,61,058

However, it is the contention of the assessee that the said particulars have been furnished in accordance with the requirements of the Companies Act and would not represent the expenditure in foreign currency incurred towards technical services rendered outside India as company is not at all involved in rendering technical services outside India. The Tribunal has proceeded to hold that since the assessee company has engaged in the development of software only, the question of incurring any expenditure in foreign currency or for providing technical services outside India would not arise and therefore, expenses incurred in foreign currency has rightly been included to turnover to arrive at deduction under s. 80HHE of the Act. The said finding is clearly erroneous. Though it is true that abovesaid particulars have been furnished by the assessee company regarding expenditure incurred in foreign currency during the relevant assessment years, the certificate is required to be given by the chartered accountant under s. 80HHE(4) of the Act r/w r. 18BBA(7) of the IT Rules. As per the certificate issued for the abovesaid assessment years, it is clear that the income that is received from export of computer software or its transmission to a place outside India is shown as nil as no figure is mentioned against the said column and under serial No. 3(11) regarding providing technical services outside India in connection with the development or production of computer software, the amount is mentioned and the amount of eligible deduction under s. 80HHE is arrived at after including the said expenses and therefore the said certificate issued by the chartered accountant of the assessee itself would show that for the abovesaid assessment years, the amount was received for providing technical services outside India in connection with development of computer software and not in connection with export of computer software or its transmission to a place in India. The Tribunal has failed to consider the said relevant documents which would clearly show that the expenses incurred in foreign exchange was towards technical services rendered outside India and not for development of software outside India. The Tribunal has proceeded on the basis accepting the contention of the assessee that software is required to be developed outside India and amount spent in foreign exchange is towards development and export of the

software at site and the same is to be included in the turnover is clearly erroneous and contrary to the certificate issued by the chartered accountant of the assessee for the abovesaid assessment years. The said certificate would show that only for the asst. yrs. 1997-98, the amount incurred in foreign exchange is shown towards export turnover relating to transmission to a place outside India and no amount has been shown towards providing technical services outside India in connection with development of software. Therefore, Tribunal was not at all justified in holding that the expenses incurred in foreign currency is not towards rendering technical services outside India but towards development and export of the software and the same is liable to be set aside and once it is held that expenditure incurred for the abovesaid assessment years pertains to technical services outside India, the same has to be excluded from the turnover for the purpose of arriving at the deduction admissible under" s. 80HHE of the Act. Accordingly, we answer the said substantial question of law about admissibility of deduction under s. 80HHE in favour of the Revenue and against the assessee in all these appeals.

Substantial question of law regarding membership of the club :

9. The substantial question of law as to whether the amount spent towards acquiring membership of the club is revenue or capital expenditure has already been answered by us in the connected appeals in IT Appeal Nos. 2975 of 2005 and connected cases, disposed of on 21st Oct., 2011 wherein the said question is answered against the Revenue and in favour of the assessee upholding the order of the Tribunal that the said expenditure is revenue in nature.

Substantial question of law regarding contribution made to traffic police :

10. So far as the finding of the Tribunal that contribution of Rs. 6.93 lakhs made towards traffic regulation can be claimed as deduction is also not justified as it is well settled that in order to claim deduction under s. 37 of the Act, the expenditure should be wholly for the purpose of business of the assessee and it is well settled that it is the duty of the police to regulate the traffic and the amount spent towards regulation of traffic can at the most be considered as donation as rightly held by the AO and cannot qualify as deduction under s. 37 of the Act. We are also supported by the decision of the Division Bench of this Court in CIT vs. M.N. Swaminathan (Decd.) by LRs (2010) 47 DTR (Kar) 359 wherein it is held that contribution made to traffic police would not qualify for deduction under s. 37 of the Act, Therefore, the said question of law is answered against the assessee and in favour of the Revenue.

Substantial question of law (2) and (3) in IT Appeal No. 2973 of 2005 :

11. These questions involve validity of the order of the Tribunal holding that the expenses of Rs. 15,89,613 incurred by the assessee towards brick works, cement, plastering, painting walls, laying ceramic tiles, MS grill, internal sanitary fixtures, sewerage works, supply and fixing of water supply pipes on the leased premises etc. would not amount to major repairs. The AO held that the said

expenditure of Rs. 15,89,613 incurred on the extensive repairs are enduring in nature and therefore it should be treated as capital expenditure in view of the decision of the Hon"ble Supreme Court in *Ballimal Naval Kishore & Anr. vs. CAT* (supra). The appellate authority held that the said expenditure incurred by the assessor towards renovation of the premises taken by it on lease for a period of six years, no advantage of enduring benefit is derived. The appellate authority further held that the said repairs are carried out by the assessee in a leased building for the purpose of business and confirmed the order passed by the AO holding that the expenditure incurred by the assessee is capital expenditure. However, allowed the depreciation at the rate applicable to the buildings. However, Tribunal has held that the said expenditure is not of any enduring nature and having regard to the explanation offered by the assessee that the premises required repairs when it was taken on lease and in order to improve the ambience of the office of the assessee to be housed, it was necessary to carry out the repairs as the same was necessary for the purpose of business specially in the business of software where there is stiff competition and mere fact that enduring benefit itself would not be a factor to be decided as to whether it is a capital or revenue expenditure. The Tribunal has held that the said amount cannot be said to be a capital expenditure and is only a revenue expenditure and decision of the Supreme Court in *Ballimal's* case cited supra is not applicable to the facts of the case.

12. It is clear from the scrutiny of the material on record that expenditure incurred by the assessee towards repairs and renovation of the premises to house the office of the assessee cannot be said to be capital expenditure having regard to the facts of the case. As it is clear that the premises had been taken on lease; it required extensive repairs and renovation and the same has been done in connection with the business of the assessee to improve the ambience of the office and expenditure was revenue in nature and the expenditure was wholly for the purpose of business as the premises had been taken on lease. The mere fact that it was taken on lease for six years would not itself render expenditure capital in nature. The decision of the Supreme Court in *Ballimal's* case referred to supra is not helpful to the Revenue in the present case as in the said case, the premises that was purchased was a ginning factory and the said factory was converted into a cinema theatre by extensive repairs and by expending substantial amount towards machinery, new furniture, replacement of electrical wiring, sanitary fittings etc., in addition to extensive repairs to the walls, to the hall, to the flooring and roofing, to doors and windows and to the stage sides and having regard to the consideration amount for which the property was purchased and the amount of repairs carried out, the Hon"ble Supreme Court has held that expenditure was capital in nature as there was enduring benefit to the property. However, in the present case, premises has been taken on lease by the assessee and the repairs that are carried out for the purpose of business to create ambience and to carry out repairs to use the premises as the office of the assessee as there was strict competition in the business of the assessee and the

expenditure of the said amount of Rs. 15,89,613 which would come to Rs. 9 per sq. ft. in respect of 17113 sq. ft. cannot at all be said to be capital expenditure and therefore, finding of the Tribunal is justified and cannot be said to be arbitrary. Having regard to the facts of the case the said finding of fact is justified and does not suffer from any perversity or arbitrariness so as to call for interference in this appeal. Accordingly, the said substantial question of law is answered against the Revenue and in favour of the assessee. Accordingly, we pass the following :

ORDER

IT Appeal Nos. 2972 of 2005 and 2974 of 2005 are allowed. The order passed by the Tribunal in ITA No. 794/Bang/1998 and 795/Bang/1998 dt. 31st March, 2005 is set aside.

IT Appeal No. 2973 of 2005 is allowed. The order passed by the Tribunal in ITA No. 793/Bang/1998 dt. 31st March, 2005 insofar as it relates to allowing the deduction under s. 80HHE of the Act and allowing the deduction in respect of contribution made to traffic police for regulating traffic is set aside and the order of the Tribunal is confirmed in all other respects.