

(2002) 08 BOM CK 0012

In the Bombay High Court

Case No : IT Appeal No's. 1303 and 1304 of 2000 14 August 2002

Commissioner of Income Tax

APPELLANT

Vs

Asea Ltd.

RESPONDENT

Date of Decision : 14-08-2002

Acts Referred:

Income Tax Act, 1961 — Section 260A, 35AB

Citation : (2002) 124 TAXMAN 598

Hon'ble Judges : S.H. Kapadia, J;J.P. Devadhar, J

Bench : Full Bench

Advocate : R.V. Desai and P.S. Jetly, for the Appellant;

Judgement

S.H. Kapadia, J.

Both the above appeals raise common questions of law and, therefore, they were heard together on 7-8-2002.

2. The questions of law framed by the department in the memo of appeal are as follows :

1. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in confirming the order of the Commissioner (Appeals) allowing investment allowance on technical know-how fees when as per the provisions of section 35AB, technical know-how fee is allowable as revenue expenditure in 6 yearly equal installments ?

2. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in confirming the order of the Commissioner (Appeals) allowing the assessee's claim in respect of provision for bad and doubtful debts and interest thereon, even though the same was not written off and no debit was made to the profit and loss account and no credit to the debtor's account and the provisions of section 36(1)(vii) were not attracted?

3. For the sake of convenience, facts in Appeal No. 1303 of 2000 are mentioned

hereinbelow.

4. On 30-5-1988, a revised return was filed by the assessee for Rs. 26,97,495 in respect of the accounting year 1987-88 corresponding to the assessment year 1988-89. However, in this appeal u/s 260A of the Income Tax Act, 1961 (hereinafter referred to as the Act), we are concerned with only two items, viz., disallowance of depreciation and investment allowance and disallowance of bad debt.

5. As regards the first item, it was argued by the assessee before the assessing officer that the assessee was entitled to depreciation and investment allowance as the assessee had incurred expenditure on account of technical know-how fees for setting up a new factory at Bangalore. It was contended that this expenditure was for setting up a plant and, therefore, the assessee claimed depreciation and investment allowance. However, the assessing officer rejected the claim of the assessee. The assessing officer held that payment of know-how fees was not for setting up a plant. The assessing officer, however, applied provisions of section 35AB of the Act and granted deduction of 1/6 of the technical know-how fees. Being aggrieved, the assessee carried the matter before the Commissioner (Appeals). The Commissioner (Appeals) came to the conclusion that in view of the Explanation to section 35AB, the words "know-how" would mean technological or industrial information which was likely to assist production of goods or manufacture of goods. It was held that for the purposes of section 35AB, know-how was a technique or information which was to be used as an aid to production. On facts, the first appellate authority found that in the present case the expenditure was capitalised. That, it was incurred much prior to the commencement of the manufacture. It was found on facts by the first appellate authority that since the expenditure was incurred prior to the commencement of manufacture, it cannot be said that the expenditure was incurred for the purposes of business. On facts, the first appellate authority found that expenditure was incurred for setting up the plant. In the circumstances, the first appellate authority came to the conclusion that section 35AB was not applicable and, accordingly, the first appellate authority allowed the claim of the assessee for depreciation and investment allowance. Being aggrieved, the revenue went in appeal. The appeal has been dismissed. Being aggrieved by the decision of the Tribunal, the revenue has filed the present appeal u/s 260A.

6. In the present appeal, the department has not challenged the findings of fact recorded by the first appellate authority and the Tribunal, viz., that the expenditure incurred was capitalised; that it was incurred before commencement of the manufacture; that section 43(3) of the Act would apply and, therefore, we are required to decide this appeal in the light of the factual findings given by the first appellate authority and the Tribunal. In the case of Scientific Engineering House (P) Ltd. Vs. Commissioner of Income Tax, Andhra Pradesh, , the Supreme Court has laid down that where a capital asset of technical know-how was acquired by the assessee, then such capital asset became a tool of the

assessee's trade with which he carried on his business. In that case, the assessee entered into collaboration agreement with a foreign company for manufacture of microscopes. Under that agreement, the foreign collaborator agreed to supply to the assessee all technical knowhow required for the manufacture of microscopes. The question which arose before the Supreme Court was whether the documentation supplied by the foreign collaborator to the assessee in the form of drawing, charts, plans constituted a book and fell within the definition of the word "plant" in section 43(3). The Supreme Court answered that question in the affirmative and in favour of the assessee. The Supreme Court held that the purpose of giving such documentation service was to enable the assessee to undertake trading activity of manufacturing microscopes. It was found on facts that with the aid and assistance of these documents the assessee was able to commence its manufacturing activity and the said documents formed the basis for manufacturing the microscopes. The Supreme Court observed that, by themselves the documents did not perform mechanical operations but that did not militate against the documents being treated as a plant since they were the basic tools of trade of the assessee and, therefore, the technical know-how was a capital asset acquired by the assessee and, therefore, such technical know-how fell within the definition of the word "plant" in section 43(3) and was, therefore, a depreciable asset. Applying the ratio of this judgment of the Supreme Court to the facts of our case, the two authorities below have found on facts that the assessee had incurred the above expenditure towards technical know-how fees. That, these technical know-how fees were paid for setting up a plant at Bangalore for manufacture of a new range of products. In the circumstances, the judgment of the Supreme court in the case of Scientific Engg. House (P) Ltd. (supra) is squarely applicable to the facts of the case. In the circumstances question No. 1 referred to above is answered in the affirmative, i.e., in favour of the assessee and against the department. Therefore, the assessee has been rightly given the benefit of depreciation and investment allowance. However, before concluding it may be mentioned that the assessee has also asked for deduction of 1/6 over a period of six years u/s 35AB but the same has been disallowed on the ground of non-applicability of section 35AB which was pressed into service by the assessing officer in his assessment order. It was held by the Tribunal that section 35AB applies to acquisition of know-how for product improvement. We leave this question open. The assessee has not come, in appeal against this finding.

7. Now coming to question No. 2, the assessing officer disallowed bad debts on the ground that the assessee had made only a provision which was not equivalent to a write-off. Being aggrieved, the assessee went in appeal to the Commissioner (Appeals) who took the view following the judgment of the Gujarat High Court in the case of Vithaldas H. Dhanjibhai Bardanwala Vs. Commissioner of Income Tax, Gujarat-V, that even a provision for bad debt could be treated as a write-off. This view of the first appellate authority was confirmed by the Tribunal. Being aggrieved, the revenue has come in appeal u/s 260A to this court.

8. As stated above, in this appeal, we are concerned with the accounting year 1987-88 relevant to the assessment year 1988-89. At this stage, it may be mentioned that section 36(1)(vii) stood amended by addition of an Explanation with effect from 1-4-1989 which, inter alia, states that any bad debt written-off as irrecoverable in the accounts of the assessee shall not include any provision for bad and doubtful debts made in the accounts of the assessee. This amendment came into force with effect from 1-4-1989 and, therefore, it does not apply to the facts of the present case. However, this amendment indicates that before 1-4-1989 even a provision for bad debt in the account of the assessee could be treated as a write-off. In the case of *Vithaldas H. Dhanjibhai Bardanwala* (supra), one of the questions which arose for determination before the Gujarat High Court was whether the Tribunal was right in holding that the bad debts of Rs. 54,145 and Rs. 10,807 for the assessment years 1967-68 and 1969-70 were not written off as per section 36 of the Act. It was argued on behalf of the department that there was a difference between writing-off an actual debt and making a provision for the same. It was argued on behalf of the department that in that case, the assessee had only made a provision and had not actually written off the debt. In that case, the assessee had debited the amount to profit and loss account/expense account but had not effected a corresponding credit to the debtor's account and, therefore, it was argued on behalf of the assessee that there was no writing-off of an actual debt. That, the assessee had only provided for writing-off. In that matter, the assessee had debited the profit and loss account of the relevant years and had credited the same to bad debt reserve account. The department argued that the assessee had forfeited its right to claim deduction u/s 36(1)(vii) by not squaring off the accounts of the concerned parties in its books. This argument of the department was rejected by the Gujarat High Court following the judgment of the Bombay High Court in the case of *Commissioner of Income Tax and Excess Profits Tax, Central, Bombay Vs. Jwala Prasad Tiwari*, in which it has been held that it was open to the assessee to debit the profit and loss account and credit the amount to the client debtor's account or it was open to the assessee to debit the profit and loss account and make corresponding entry in another appropriate account like suspense account. That, there was nothing in section 10(2)(xi) equivalent to section 36(2)(i)(b) which lays down that the amount should be written off in the account of the debtor. What the section required was that the amount should be written off in the books of the assessee. That, the section nowhere lays down that the amount should be written off by debiting the profit and loss account of the assessee and crediting the amount to the account of the debtor. In view of the said judgments, question No. 2 is answered in the affirmative, i.e., in favour of the assessee and against the department.

9. For above reasons, both the appeals are dismissed with no order as to costs.