

(2012) 05 DEL CK 0653

In the Delhi High Court

Case No : ITA 55 of 2012 and 57 of 2012

Commissioner of Income Tax

APPELLANT

Vs

Havells India Ltd.

RESPONDENT

Date of Decision : 21-05-2012

Acts Referred:

Income Tax Act, 1961 — Section 195, 260A, 40, 9, 9(1)

Citation : (2012) 5 AD 755 : (2012) 253 CTR 271 : (2013) 352 ITR 376 :
(2012) 208 TAXMAN 114

Hon'ble Judges : Sanjiv Khanna, J;R.V. Easwar, J

Bench : Division Bench

Advocate : Sanjeev Sabharwal, for the Appellant; Ajay Vohra, Ms. Kavita Jha and Mr. Somnath Shukla, for the Respondent

Judgement

R.V. Easwar, J.—These are two appeals filed by the Revenue u/s 260A of the Income Tax Act, 1961 ("Act", for short). They relate to the assessment year 2005-06. Both the appeals arise out of the common order passed by the Income Tax Appellate Tribunal on 27.05.2011 in cross appeals filed by the assessee and the Revenue in ITA No. 1300/Del/2010 and ITA No. 2093/Del/2010 respectively. The following substantial questions of law were framed by us: -

1. Whether the Income Tax Appellate Tribunal is right in holding that Section 40(a)(ia) of the Income Tax Act, 1961 is not applicable to testing fee of Rs. 14,71,095/- paid to M/s. CSA International, Chicago as there was no failure on the part of the respondent-assessee to deduct tax at source?

2. Whether the Income Tax Appellate Tribunal was right in holding that the pre operative expenses of Rs. 2,31,253/- can be allowed as a revenue expenditure?

3. Whether expenditure of Rs. 92,67,841/- incurred by the Assessee on fully convertible debenture issue is revenue expenditure or capital expenditure?

2. We are concerned with the assessment year 2005-06. The assessee is a company engaged in the manufacture of switch gears, energy meters, cables and

wires, electrical fans, compact florescent lamp and related components. It also trades in luminaires, lighting fixtures and exhaust fans.

3. As regards first substantial question of law, the brief facts are as follows. The assessee paid a sum of Rs. 14,71,095/- to M/s. CSA International, Chicago, Illinois, USA for the purpose of obtaining witness testing of AC contractor as part of CB report and KEMA certification. The US Company had specialised knowledge and facilities for carrying out the type of testing and the necessary certification, which was required by the assessee. In the course of the assessment proceedings, the Assessing Officer noticed that the assessee had not deducted tax at source u/s 195 of the Act from the amount paid to the US Company. He accordingly proposed to disallow the payment by invoking Section 40(a)(ia) of the Act. The assessee by letter dated 04.10.2007 stated that the amount was paid as testing charges to the US Company, that the testing was carried out by the US Company outside India, that no income arose or accrued to the US Company in India and, therefore, the assessee did not deduct any tax from the amount paid. The assessee, therefore, claimed that the provisions of Section 40(a)(ia) cannot be invoked to disallow the payment on the ground of non-deduction of tax at source.

4. The Assessing Officer did not agree with the assessee's contentions. According to him the assessee was not right in saying that no income had accrued or arisen to the US Company in India. According to him the deeming provisions of Section 9(1)(vii) of the Act was applicable and that the amount paid represented fees for technical services rendered by the US Company to the assessee within the meaning of Explanation 2 below Section 9(1)(vii)(b) of the Act. According to the Assessing Officer the testing of the equipment was a highly specialised job of technical nature and, therefore, the amount paid by the assessee to the US Company represented consideration for the rendering of technical services to the assessee. He, therefore, held that the amount was assessable in the hands of the US Company as income deemed to have accrued or arisen in India and since no tax was deducted by the assessee from the remittance of the amount, Section 40(a)(ia) came into operation and thus the amount of Rs. 14,71,095/- fell to be disallowed. The Assessing Officer also referred to Article 12(4)(b) of the agreement for the avoidance of double taxation entered into between India and USA and observed that the payment was also covered under the said article as "fees for included services" as defined therein. According to the Assessing Officer, the testing report and certification represented technical services which made available technical knowledge, experience and skill to the assessee because they were utilized in the manufacture and sale of the products in the business of the assessee. In this view of the matter the Assessing Officer disallowed the amount of Rs. 14,71,095/- u/s 40(a)(ia) of the Act.

5. The assessee appealed to the CIT (Appeals) against the disallowance. The CIT (Appeals) referred to the judgment of the Kerala High Court in Cochin Refineries

Ltd. Vs. Commissioner of Income Tax, and held that the payment made by the assessee to the US Company was for obtaining technical services for the purpose of its business and such services were utilised in the manufacture and sale of the assessee's products. He accordingly agreed with the Assessing Officer that Section 195 of the Act was applicable. He, therefore, held that the amount was rightly disallowed u/s 40(a)(ia) for not being subjected to deduction of tax.

6. The assessee carried the matter in further appeal to the Tribunal in ITA No. 1300/Del/2010. Several contentions were raised before the Tribunal on behalf of the assessee. The principal contentions were: -

(a) That Section 9(1)(vii)(b) of the Act exempted from tax the fees for technical services if they were paid for services which were utilised by the assessee in a business or profession carried on outside India or for the purpose of making or earning any income from any source outside India. Since the assessee was making exports to other countries, the fees for technical services were paid for the purpose of making or earning income from a source outside India and hence the payment was not chargeable to tax in India. There was thus no liability to deduct tax.

(b) The departmental authorities erred in concluding that the technical report and certification were utilised in the manufacture and sale of the assessee's products in the assessee's business in India.

(c) The KEMA certification enables the assessee to sell its products freely in the European Union. The assessee exports the products which bear the KEMA certification and that such certification is not required in India or by the Indian buyers and the taxing authorities were wrong in saying that the technical services were utilised by the assessee for its business in India.

(d) In any case under Article 12(4)(b) of the double tax avoidance agreement between India and USA makes it a condition that the mere rendering of technical services is not sufficient and that it is also necessary, in order that the fees for included services are taxable in India, that such services should have resulted in "making available" to the assessee technical knowledge, experience and skill.

7. The Tribunal, on the basis of arguments and the materials placed before them and after referring to Section 9(1)(vii)(b) of the Act recorded the following findings:-

(a) The certification obtained by the assessee from the US Company was for enabling the export of its products.

(b) The income tax authorities have not been able to bring anything on record to support their stand that the service of testing and certification has been applied by the assessee for its manufacturing activity within India.

(c) The CIT (Appeals) has not specifically met the contention of the assessee, raised before him, that the technical services were rendered by the US Company

outside India and the assessee has also utilised them outside India and the payment was also received by the US Company outside India. The assessee's contention was that the technical services were utilised for the purpose of making or earning any income from any source outside India and was therefore covered by the second exception made in Section 9(1)(vii)(b) of the Act.

(d) The assessee has been able to show that the testing and certification were necessary for the export of its products and that these were actually utilised for such export and were not utilised for the business activities of production in India. The assessee has thus discharged its burden, whereas the Revenue has not been able to show to the contrary and they have not denied that the utilisation of the testing and certification was in respect of the exports. In view of the above findings, the Tribunal deleted the disallowance made u/s 40(a)(ia) of the Act.

8. It is against the aforesaid decision of the Tribunal that the Revenue has come in appeal before this Court. It appears to us on a reading of the orders of the departmental authorities and the order of the Tribunal that there is no dispute that the amount paid by the assessee to the US Company represented "fees for technical services" within the meaning of Section 9(1)(vii)(b) of the Act. In fact, to the specific query put by us in the course of the hearing to the learned counsel for the assessee, he frankly stated that he could not dispute this position, having regard to the wide definition of "fees for technical services" in the aforesaid provision. If that is so, the only question which we are required to examine is (a) whether the fees were payable in respect of services utilised in a business or profession carried on by the assessee outside India or (b) they were paid for the purposes of making or earning any income from any source outside India. In either of these two cases, the amount paid will not be taxable in the hands of the non-resident company and correspondingly there will be no liability upon the assessee to deduct tax u/s 195 of the Act. It was stated before us by the learned counsel for the assessee that exception (b) will be applicable in the assessee's case and not (a). In other words his contention was that the fees were payable for the purposes of making or earning income from a source outside India. He elaborated this by submitting that the certification by the US Company that the products turned out by the assessee were KEMA certified and were fit for being used in European countries and in countries where such certification is accepted, was indispensable for the export of such products to those countries and accordingly the fees for such certification and testing were for the purposes of making or earning income from a source outside India. It was accordingly contended that the conditions of the second exception in Section 9(1)(vii)(b) of the Act were satisfied.

9. In support his contention, the learned counsel for the assessee drew our attention to a judgment of the Madras High Court in *The Commissioner of Income Tax Vs. Aktiengesellschaft Kuhnle Kopp and Kausch W. Germany by BHEL*, . In this case it was held that the exports of goods represented a source

outside India. The High Court was concerned with Section 9(1)(vi) which was concerned with payment of royalty by a person resident in India to a non-resident. Though that provision was concerned with royalty, the exceptions provided from taxability of the royalty income in the hands of the non-resident are the same as in the case of fees for technical services dealt with in Section 9(1)(vii)(b) of the Act. In that case the resident company paid royalty to a West German company. The royalty was payable on export sales effected by the resident-assessee. The question before the High Court was whether the Tribunal was right in law in holding that the royalty on export sales was not taxable within the meaning of Section 9(1)(vi) of the Act. The High Court held as under: -

As far as royalty on export sales is concerned, that amount is also exempt u/s 9(1)(vi) of the income tax Act. Though the royalty was paid by a resident in India, it cannot be said that it was deemed to have accrued or arisen in India as the royalty was paid out of the export sales and, hence, the source for royalty is the sales outside India. Since the source for royalty is from the source situate outside India, the royalty paid on export sales is not taxable. The Appellate Tribunal was therefore correct in holding that the royalty on export sales is not taxable within the meaning of section 9(1)(vi) of the income tax Act.

10. The judgment of the Madras High Court certainly supports the contention of the learned counsel for the assessee. In an earlier judgment in *Commissioner of Income Tax Vs. Anglo French Textiles*, a Division Bench of the Madras High Court had occasion to consider a somewhat similar question arising u/s 9 of the Act. In that case the assessee was a company incorporated under the French laws which were applicable to possessions in Pondicherry in India. It had a textile mill in Pondicherry and its activity consisted in the manufacture of yarn and textiles as well as export of textiles from Pondicherry. The entire business operations were confined to the territory of Pondicherry. After the merger of Pondicherry with India in August, 1962, the Income Tax Act was extended to Pondicherry w. e. f. 1.4.1963. Till then, the French law relating to income tax was in force in Pondicherry. During the period when the French tax law was in force, the assessee surrendered certain raw cotton import and machinery import entitlement and received payments from the Textile Commissioner (Bombay). The question arose as to the taxability of the income referable to the import entitlements. While the income tax department took the stand that the income accrued to the assessee outside Pondicherry and was therefore taxable under the Act, the assessee maintained that the receipts were only in Pondicherry and since the exports were made from Pondicherry, the income accrued or arose to the assessee in the territory of Pondicherry which was outside the purview of the Act. The Madras High Court observed that the import entitlements arose out of the export activity which was carried on by the assessee only in Pondicherry, that no part of the manufacturing or selling activity of the assessee was carried on outside Pondicherry, that the import entitlements were relatable only to the export performance which took place in Pondicherry and that on the fulfillment of the export activity, a right to receive the export incentive accrued in favour of the

assessee in the territory of the Pondicherry. The argument of the department was that the incentive was quantified and sent from Bombay from the office of the Textile Commissioner and, therefore, the income arose within the taxalite territories. This argument was rejected by the Madras High Court by holding that "the right to receive the import entitlements arose when the export commitment was fulfilled by the assessee in Pondicherry, though such amount was subsequently ascertained or quantified". It was also argued on behalf of the Revenue before the High Court that the import entitlement should be regarded as a source of income in the taxable territories and u/s 9(1) of the Act, the income arising out of the encashment of the import entitlements should be deemed to accrue or arise in the taxable territories. This argument was also rejected by the Madras High Court which held: -

Equally, it is difficult to regard the import entitlements as a source of income which should be looked at from a practical view-point and not merely as an abstract legal concept. We are, therefore, unable to agree with the contention of the learned counsel for the Revenue that the import entitlements constituted a source of income within the meaning of Section 9 of the Act as to deem the import entitlements as having accrued or arising in India.

This earlier judgment of the Madras High Court does not appear to have been brought to the notice of the Division Bench which decided the later case. The observations of the Madras High Court in the earlier case, which we have quoted above, clearly suggest that the export activity or export sales were the source of the import entitlements and the export activity took place in Pondicherry and it was only on fulfillment of the export activity that a right to receive the import entitlement/ incentive accrued in favour of the assessee. Since the export activity was fulfilled in Pondicherry, the source of income was located in Pondicherry. Applying this judgment to the facts before us in the present case, we have to conclude that the export activity having taken place or having been fulfilled in India, the source of income was located in India and not outside. Moreover, just as in the Madras case it was held that the mere fact that the import entitlements which had their source in Bombay, did not constitute a source of income within the meaning of Section 9 of the Act, we have also to hold in the present case that the mere fact that the export proceeds emanated from persons situated outside India did not constitute them as the source of income.

11. The question as to what is a source of income has been dealt with in some authoritative pronouncements. The Judicial Committee in *Rhodesia Metals Ltd. v. Commissioner of Income Tax*, (1941) 9 ITR (Suppl.) 45 observed that a "source" means not a legal concept but one which a practical man would regard as a real source of income. This observation was adopted by Malik, J. in his separate but concurring judgment in the case of *RANI AMRIT KUNWAR Vs. COMMISSIONER OF INCOME TAX, C.P. and U.P.*, , a decision of the Full Bench of the Allahabad High Court. A source of income was described by R. S. Pathak, J. (as he then was) in

the following words in Seth Shiv Prasad Vs. Commissioner of Income Tax, at page 18: -

A source of income, therefore, may be described as the spring or fount from which a clearly defined channel of income flows. It is that which by its nature and incidents constitutes a distinct and separate origin of income, capable of consideration as such in isolation from other sources of income, and which by the manner of dealing adopted by the assessee can be treated so.

The observations of the Judicial Committee (*supra*) as to what is a source of income have been approved by the Supreme Court in Commissioner of Income Tax, Madhya Pradesh, Nagpur and Bhandara Vs. Lady Kanchanbai and Another, . The location or situs of a source of income is another aspect. The third aspect is the accrual of the income. Though it is true, as held by Kania, C.J., speaking for a Constitution Bench of the Supreme Court in COMMISSIONER OF Income Tax, BOMBAY Vs. AHMEDBHAI UMARBHAI and CO., BOMBAY., at page 479, that the place where the source of income is located may not necessarily be the place where the income also accrues, that question is not material in the present case because herein we are concerned only with the question as to the location of the source. The real question is whether the export sales proceeds received from goods manufactured and exported from India constitute a source inside or outside India. To decide the same we have to take a pragmatic and a practical view and not approach the question from a theoretical perspective.

12. Section 9(i)(vii)(b) contemplates a source located outside India. It is difficult to conceptualise the place/ situs of the person who make payment for the export sales as the source located outside India from which assessee earned profits. The export contracts obviously are concluded in India and the assessee's products are sent outside India under such contracts. The manufacturing activity is located in India. The source of income is created at the moment when the export contracts are concluded in India. Thereafter the goods are exported in pursuance of the contract and the export proceeds are sent by the importer and are received in India. The importer of the assessee's products is no doubt situated outside India, but he cannot be regarded as a source of income. The receipt of the sale proceeds emanate from him from outside India. He is, therefore, only the source of the monies received. The income component of the monies or the export receipts is located or situated only in India. We are making a distinction between the source of the income and the source of the receipt of the monies. In order to fall within the second exception provided in Section 9(1)(vii)(b) of the Act, the source of the income, and not the receipt, should be situated outside India. That condition is not satisfied in the present case. The Tribunal, with respect, does not appear to have examined the case from this aspect. Its conclusion that the technical services were not utilised for the assessee's business activity of production in India does not bring the assessee's case within the second exception in Section 9(1)(vii)(b) of the Act. It does not bring the case under the first exception either, because in order to get the benefit of the first

exception it is not sufficient for the assessee to prove that the technical services were not utilised for its business activities of production in India, but it is further necessary for the assessee to show that the technical services were utilised in a business carried on outside India. Therefore, we cannot also approve of the Tribunal's conclusion in para 29 of its order to the extent it seems to suggest that the assessee satisfies the condition necessary for bringing its case under the first exception. Be that as it may, as we have already pointed out, since the source of income from the export sales cannot be said to be located or situated outside India, the case of the assessee cannot be brought under the second exception provided in the Section.

13. Mr. Vohra, learned counsel for the assessee, however, contended that income arose not only from the manufacturing activity but also arose because of the sales of the products and if necessary a bifurcation of the income should be made on this basis and that portion of the income which is attributable to the export sales should qualify for the second exception. This argument is only a limb of the main contention that the income arises from the export sales and the source of the income is located outside India. We have already expressed our difficulty in accepting that argument. It is true that the profits arise both from the manufacturing activity and from the sale. There are several authorities dealing with this question in the context of cases where an assessee had its manufacturing facility in British India but sold the goods outside British India. In such cases, it has been held that the profits arose both from manufacture and the sales and that part of the profit which arises from sales outside British India would be exempt from tax: See *ANGLO-FRENCH TEXTILE COMPANY, LTD. Vs. COMMISSIONER OF Income Tax, MADRAS* : NO. 2., *CIT v. Ahmedbhai Umarbhai & Co.* (supra). But these cases are not of any assistance to the assessee in the present case since the contention here is that the source of income is the export sales and the export sales are located outside India.

14. For these reasons we are unable to hold that the assessee's case falls under the second exception provided in Section 9(1)(vii)(b) of the Act. In other words, we are unable to accept that the fees for technical services were paid by the assessee to the US Company for the purpose of making or earning any income from any source outside India.

15. The result of our discussion is that the fees for technical services are taxable in the hands of the US Company under the provisions of the Act. The question to be considered then would be whether there is anything in the agreement for avoidance of double taxation between India and USA which would exempt or reduce the burden of taxation in respect of the fees for technical services received by the US Company. This aspect of the matter has not been examined by the Tribunal, though raised before it by the assessee, since there was no occasion for the Tribunal to do so on account of the view it took regarding the taxability of the fees for technical services under the Act. It is axiomatic that if the receipt is not taxable under the Act, then there is no need to examine

whether it would fall under any of the provisions of the agreement for avoidance of double taxation. We cannot therefore find fault with the Tribunal for not having discussed the applicability of Article 12 of the Indo-US Treaty, which defines "fees for included services" in a manner which is different from the definition of "fees for technical services" in Explanation 2 below Section 9(1)(vii) of the Act. It would therefore not be proper or necessary for us to examine the applicability of the treaty which should be left to the Tribunal. While therefore answering the first substantial question of law in the negative, in favour of the Revenue and against the assessee, we restore the issue relating to the applicability of the Indo-US treaty to the receipt in question and consequently the applicability of Section 40(a)(ia) of the Act to the Tribunal.

16. As regards the second substantial question of law, the brief facts are as follows. In the course of the assessment proceedings it was noticed by the Assessing Officer that the assessee had undertaken a project at Haridwar for installing a unit engaged in the manufacture of fans, etc. and that in the books of accounts it has been capitalising the expenses incurred towards the project as capital works in the progress. The total of such expenses incurred up to the end of the accounting year relevant to the assessment year 2005-06 was Rs. 2,31,253/- . In the computation of income the assessee had claimed the expenses as a deduction on the ground that these were expenses incurred in the course of its regular business and were related to the expansion of the existing business. The Assessing Officer, relying on the accounts of the assessee, held that the expenses should be treated as capital in nature since the Haridwar Unit was not dependent on the existing business of the assessee and vice-versa. Applying the test of the closure of one business not affecting the continuance of the other and relying on some authorities, the Assessing Officer disallowed the expenditure as capital in nature.

17. On appeal, the CIT (Appeals) examined the details of the expenses and found that they represented salaries, travelling expenses and other commercial expenses in connection with the expansion of the existing business. According to the CIT (Appeals), there was no provision in the Act permitting the allowance of the expenses mentioned above during the construction period or during the period before the assets were first put to use. He noted that the assessee was not able to substantiate the contention that it was only a case of expansion of the existing business and was not able to lead evidence regarding interlacing and interdependence between the existing and new units. He further noted that in the accounts the assessee had capitalised the expenses. In this view of the matter he upheld the disallowance.

18. The assessee carried the matter in further appeal before the Tribunal. The Tribunal examined the director's report, the financial statements and the notes appended thereto etc. and found that there was complete interlacing and intermingling of the funds of the assessee in all its units besides there being a common management. The Tribunal also referred to the judgment of this Court

in CIT v. Monnet Industries Ltd., (2009) 221 CTR 266 and applying this decision to the facts found, it held that the expenditure was revenue in nature having been incurred for the expansion of the existing business and accordingly directed the Assessing Officer to allow the same as deduction.

19. Having heard both the sides on this question, we are satisfied that the Tribunal has taken the right view of the matter. There is no challenge to the factual findings recorded by the Tribunal on the basis of the financial statements and the director's report before them, to the effect that (a) that the Haridwar Unit was only a expansion of an existing business of the assessee and (b) that there was intermingling and interlacing of the funds of the Units and (c) there was a common management. This is the usual test which has been deduced by the Courts in India, following the locus classicus on the subject, which is that of the House of Lords in the case of Scales v. George Thompson & Co. Ltd., 13 TC 83 where the test laid down by Rowlatt, J. was whether there was interconnection, interlacing, interdependence and a unity embracing the different businesses. If this test is answered in the affirmative, all the businesses constituted the same or single business with the result that expenditure incurred by the assessee in respect of the expansion of an existing business would fall to be considered as revenue expenditure. The fact that in the books of account the assessee had capitalised the expenses does not prevent the assessee from claiming them as revenue expenses since the question of allowance of expenses has to be considered in the light of the legal position and the accounting treatment cannot be conclusive. In the present case considering the undisputed factual findings of the Tribunal, the substantial question of law is answered in the affirmative, in favour of the assessee and against the Revenue.

20. We may now turn to the third question. The brief facts in this connection are as follows. During the relevant previous year, the assessee issued 4% fully convertible debentures amounting to Rs. 2350 lakhs comprising of 235 debentures of the face value of Rs. 10 lakhs each to another company by name M/s. Shine Ltd. which was incorporated under the laws of Mauritius. The issue of debentures was to give effect to the investor agreement entered into with the Mauritius Company. Necessary amendments were made to the Articles of Association of the assessee-company. In connection with the debentures issued the assessee had incurred the following expenditure: -

(i)

Paid to M/s. Price Water House Coopers (P) Ltd.

5332500/-

(ii)

Paid to M/s. WadiaChandy & Co.

639450/-

(iii)

Payment M/s. KPMG India Pvt. Ltd.

4,88,768/-

Total

64,60,718/-

21. In addition to the aforesaid expenditure, the assessee also paid interest of Rs. 28,07,123/- on the debentures in the relevant previous years. The aggregate of all the four items of expenditure came to Rs. 92,67,841/- .

22. The above expenditure was claimed as revenue expenditure in the return of income. The Assessing Officer was of the view that the debenture issue was in fact an issue of equity share capital to the Mauritius Company and accordingly the entire expenditure should be disallowed as capital expenditure. In support of this conclusion he referred to the board resolution in which it was stated that the FCDs would be converted into equity shares on or before 12.06.2006 and these shares would be issued to the Mauritius Company. It was also mentioned in the resolution that the Mauritius Company would be entitled to bonus shares in the ratio of 1:1 and they will be allotted at the time of conversion of the debentures. According to the Assessing Officer, this actually meant that the assessee was in fact making an issue of share capital and according to the judgments of the Supreme Court in *Brooke Bond India Limited Vs. Commissioner of Income Tax, West Bengal-III*, *Calcutta*, and *Punjab State Industrial Development Corporation Ltd., Chandigarh Vs. Commissioner of Income Tax, Patiala*, any expenditure incurred in relation to the expansion of the capital base of a company should be treated as capital expenditure. He accordingly disallowed the expenditure of Rs. 92,67,841/- .

23. On appeal the CIT (Appeals) referred to the judgment of the Rajasthan High Court in *Commissioner of Income Tax Vs. Secure Meters Ltd.,*) in which it was held that the position has to be examined only with reference to the time when the debentures were issued and that the fact that at a future point of time they were to be converted into shares was irrelevant in order to decide the allowability of the expenditure incurred in connection with the debenture issue, and allowed the expenditure as revenue expenditure. He also noted that the SLP filed by the revenue against the judgment of the Rajasthan High Court (*supra*), was dismissed on 11.08.2009. He accordingly directed the Assessing Officer to allow the expenditure as revenue expenditure. His decision was affirmed by the Tribunal in the appeal by the revenue in ITA No. 2093/Del/2010.

24. The Revenue is in appeal. The main contention on its behalf is that the position should be seen not only with reference to time at which the debentures are issued but the fact that at a future point of time they were to be converted in shares should also be taken note of in order to judge the allowability of the expenditure incurred in connection with the debenture issue. It was submitted

that on the facts of the present case, the debentures were to be converted within a period of 15 months, that is on or before 12.06.2006, and that the assessee company had even fixed the price at which the shares would be issued upon conversion of the debentures, and that even the issue of bonus shares had been finalised at the time of the debenture issue and all these facts clearly showed that the issue was in truth and effect only an issue of share capital. It was accordingly contended that the judgments of the Supreme Court cited supra were squarely applicable.

25. It is well settled that expenditure incurred in connection with the issue of debentures or obtaining loan is revenue expenditure. Reference in this connection may be made to the leading judgment of the Supreme court in *India Cements Ltd. Vs. Commissioner of Income Tax, Madras*, The question before us however, is whether it is a debenture issue or an issue of share capital involving the strengthening of the capital base of the company. Though it prima facie appears that there are sufficient facts to indicate that what was contemplated was an issue of shares to the Mauritius Company under the Investor Agreement which would result in strengthening of the assessee's capital base, having regard to the judgments cited on behalf of the assessee, in which it has been held that despite indications to the effect that the debentures are to be converted in the near future into equity shares, the expenditure incurred should be allowed as revenue expenditure on the basis of the factual position obtaining at the time of the debenture issue, we are not inclined to take a different view. The following cases have been cited on behalf of the assessee in support of the view that even in such a situation the expenditure is allowable as revenue expenditure: -

- (i) *Commissioner of Income Tax Vs. East India Hotels Ltd.*,
- (ii) *The Commissioner of Income Tax and The Deputy Commissioner of Income tax (Asst.) Special Range-5 Vs. ITC Hotels Ltd.*,
- (iii) *The Commissioner of Income Tax Vs. South India Corporation (Agencies) Limited*,
- (iv) *Commissioner of Income Tax Vs. First Leasing Co. of India Ltd.*,

26. In addition to the above judgments, we also have the judgment of the Rajasthan High Court (supra) against which the SLP filed by the Revenue was dismissed. Having regard to the predominant view taken in the above judgments, in which the judgment of the Supreme Court in *India Cement* (supra) has been noticed, we are inclined to uphold the view taken by the Tribunal that the expenditure is revenue in nature. Accordingly, we answer the substantial question of law in favour of the assessee and against the revenue. In the result the appeals filed by the revenue are disposed of with no order as to costs.