

आयकर अपीलीय अधिकरण] पुणे न्यायपीठ "बी" पुणे में
IN THE INCOME TAX APPELLATE TRIBUNAL
PUNE BENCH "B", PUNE

BEFORE MS. SUSHMA CHOWLA, JM AND
SHRI ANIL CHATURVEDI, AM

आयकर अपील स० / ITA No.1070/PUN/2013

निर्धारण वर्ष / Assessment Year : 2008-09

Jain Irrigation Systems Ltd.,
N.H.No.6, Bambhori,
Jalgaon – 425001.

..... अपीलार्थी /
Appellant

PAN : AAACJ7163Q.

बनाम v/s

Dy.Commissioner of Income Tax,
Income Tax Office,
Jalgaon – 425001.

..... प्रत्यर्थी /
Respondent

Assessee by : Shri Nikhil Pathak.

Revenue by : Shri Dr. Vivek Aggarwal.

सुनवाई की तारीख / Date of Hearing : 07.12.2017	घोषणा की तारीख / Date of Pronouncement: 28.02.2018
---	---

आदेश / ORDER

PER ANIL CHATURVEDI, AM :

1. This appeal filed by the assessee u/s 253 of the Act is emanating out of the order of Commissioner of Income Tax (A) – II, Nashik dt. 19.03.2013 for the assessment year 2008-09.

2. The relevant facts as culled out from the material on record are as under :-

2.1 Assessee is a company stated to be engaged in the business of manufacture of Irrigation Systems, Sprinklers System, PVC Pipes and

fittings etc. Assessee filed its return of income for A.Y. 2008-09 declaring total income of Rs.Nil and carry forward loss of Rs.174,74,91,269/-. The case was selected for scrutiny and thereafter assessment was framed u/s 143(3) of the Act vide order dt.19.12.2011 and the total income before setting up of losses was determined at Rs.1,88,19,97,609/-. Aggrieved by the order of AO, assessee carried the matter before Ld.CIT(A), who vide order dt.19.03.2013 (in appeal No.Nsk/CIT(A)-II/429/11-12) granted partial relief to the assessee. Aggrieved by the order of Ld.CIT(A), assessee is now in appeal before us and has raised the following grounds :

“1. Disallowance of premium of Rs.4,94,72,088 on redemption of preference shares

1.1 The learned CIT (A) erred in 'confirming the disallowance of premium' of Rs. ,94,72,088 on redemption of preference shares.

On the facts and in the circumstances of the case, the disallowance of Rs. 4,94,72,088 be cancelled.

1.2 The learned CIT (A) failed to appreciate that in the facts of the case, the character of loan had not ceased on conversion into preference shares and as such so called premium must be taken as nothing but interest/fiance cost and consequently an admissible deduction u/s. 36 (i) (iii) or u/s. 28 or u/s. 37 (1) of the Act.

1.3 The sustaining of the disallowance of Rs. 4,94,72,088 without appreciating the facts of the case and merely relying upon the preceding year's assessment cannot be sustained or justified.

2. Disallowance of Rs.17,00,630 out of interest paid

2.1 The learned CIT (A) erred in confirming the disallowance of Rs.17 ,00630 out of interest paid on account of interest free deposits given to the owners of premises.

On the facts and in the circumstances of the case the said disallowance be cancelled.

2.2. The learned CIT (A) failed to appreciate that as no rent was paid/payable, the amount of interest free deposit considering the location could not be regarded as excessive or unreasonable.

2.3 WITHOUT PREJUDICE the disallowance should be restricted to a nominal amount considering the fact that the appellant had owned funds and the cost of borrowing was around 6% p.a. only.

3. Disallowance of Rs.10,20,000 out of interest paid

3.1 The learned CIT (A) erred in confirming the disallowance of Rs.10,20,000 out of interest paid on the ground of alleged excessive unreasonable interest free deposit to Jain Bros. Industries and Drip and Pipe Suppliers in the F. Y. 2001-02.

3.2. The learned CIT (A) failed to appreciate that the estimation of 'reasonable' deposit by the AO was the result of guess work and surmises and as such no disallowance was called for.

3.3. The learned CIT (A) erred in ignoring the actual cost of borrowing which was around 6" p.a./owned funds of the appellant and consequently further erred in confirming the disallowance of interest calculated at 12% p.a.

3.4 The CIT (A) ought to have cancelled the disallowance of Rs.10,20,000 out of interest paid as there was no direct nexus between the grant of interest free deposit and borrowed funds and the fact that no disallowance was made in the past on this score.

4. Disallowance of Rs.28,87,625 out of interest paid

4.1 The learned CIT (A) erred in confirming the disallowance of Rs.28,87,625 out of interest paid on the ground of alleged excess interest free deposits to S/Shri. B. H. Jain, Ajit Jain, Ashok Jain and Smt. Nisha Jain.

On the facts and in the circumstances of the case the said disallowance be cancelled.

4.2 The disallowance of Rs. 28,87,625 being the result of guess work and surmises, could not be sustained.

4.3 The learned CIT (A) failed to appreciate that deposit shad been given in the course of and for the purpose of business only and that in the year in which there were adequate owned funds and/or cost" of borrowing was hardly around 6%p.a.

5. Disallowance of depreciation on non compete fee

5.1 The learned CIT(A) erred in confirming disallowance of depreciation of Rs.18,28,125 on compete fee.

5.2 The learned CIT (A) erroneously concluded that the on compete fee was not an intangible asset and as such not subject to depreciation.

5.3 The learned CIT (A) in fact ought to have held that the expenditure in the form of non compete fee was of revenue nature and therefore fully allowable.

5.4 Assuming two view are possible, the learned CIT (A) ought to have followed view favourable to the assessee.

6. Carry forward of losses

6.1 The learned CIT (A) on the facts and in the circumstances of the case ought to have allowed the loss of Rs. 8,24,94,154 incurred by Orient Vegetexpo Ltd., an amalgamating company as the requisite conditions had been satisfied instead of giving direction to examine the issue again.

6.2 The learned AO be directed to allow the appellant's claim for carry forward of losses/depreciation allowances including for the A.Y.1993-94, to A. Y. 1999-2000 viz. Rs.1,31,63,54,679.”

3. Before us, at the outset, Ld.A.R. submitted that assessee does not wish to press ground No.6. In view of the aforesaid submission, ground No.6 is dismissed as not pressed.

4. First ground is with respect to disallowance of premium paid on redemption of preference shares.

4.1. AO noticed that assessee had claimed expenditure of Rs.4,94,72,088/- being premium on account of redemption of 4% redeemable preference shares. AO noticed that identical issue arose in assessee's own case in A.Y. 2007-08 and the order of AO was upheld by Ld.CIT(A). He therefore, following the order of his Predecessor, disallowed the expenses of Rs.4,94,72,088/-. Aggrieved by the order of AO, assessee carried the matter before Ld.CIT(A), who confirmed the action of AO. Aggrieved by the order of Ld.CIT(A), assessee is now in appeal before us.

5. Before us, at the outset, Ld.A.R. submitted that on identical facts in assessee's own case in A.Y. 2007-08 the issue was decided against the assessee. He pointed to the relevant findings in ITA No.982/PUN/2013 dt.09.06.2017 for A.Y. 2007-08. He therefore

submitted that the issue be decided accordingly. Ld.D.R. did not object to the submissions made by Ld.A.R.

6. We have heard the rival submissions and perused the material on record. The issue in the present case is with respect to the allowability of premium paid on redemption of preference shares. We find that identical issue arose in assessee's own case in A.Y. 2006-07 and 2007-08. The Co-ordinate Bench of the Tribunal while deciding the issue in A.Y. 2006-07 in favour of Revenue had relied on the decision of Hon'ble Calcutta High Court in the case of Hindustan Gas Vs. CIT (11) ITR 549 (Cal). The decision in A.Y. 2006-07 was followed in A.Y. 2007-08. The relevant observation of the Co-ordinate Bench of the Tribunal, while deciding the issue in A.Y. 2006-07 are as under :

"4. Bringing attention to Ground No.2, where premium related issue is raised, Ld. Counsel fairly submitted that the said issue has to be decided in favour of the Revenue considering the fact that premium paid for redemption of preferential shares is of capital nature and therefore the same is not an allowable expenditure in view of the Hon'ble Calcutta High Court judgment in the case of Hindustan Gas & Industries Ltd. Vs. CIT 117 ITR 549 (Cal.).

5. *On this issue, we heard both the parties and finally Ground No.2 relating to premium paid on redemption of preferential shares is dismissed for the reasons specified by the CIT(A) in his order dated 25-06-2010. Relevant operational paragraph in this regard is extracted as under :*

"9.2 I have carefully considered the submissions of the appellant and assessment order of the A.O. It is an undisputed fact that the amount of Rs.1,18,10,000/- was paid on account of premium at the rate of Rs.47.24 per preference share. The emphasis of the appellant was that the said premium in respect of the preference shares is in the nature of interest hence allowable u/s.36(1)(iii) of the Act. It is the contention of the appellant that the said premium is covered under "similar right or obligation" of the definition of "interest" u/s.2(28A) of the Act. The arguments of the appellant are not acceptable. The appellant also placed reliance, on the decision in the case of Bombay Dyeing Manufacturing Co. Ltd. 123 ITD 1 rendered by the Mumbai Bench of the Tribunal. The Hon'ble Tribunal held that premium paid in respect of Secured Premium Notes (SPNs) is in the nature of interest and allowable as deduction. There is a

clear distinction between preference shares and SPNs. The SPNs are debt instruments whereas the preference shares are in the category of equity capital. Therefore, the reliance of the appellant on the said decision is of no use. In view of this, the argument that preference share capital is in the nature of a long-term debt is also not acceptable. The appellant also relied on the Accounting Standard 31 regarding the Financial Instruments - Presentation. A perusal of the said Accounting Standards show that the preference shares are not equated with debt instruments. They are to be shown as a liability under the head "capital". The deduction has to be considered under the Income-tax provisions and Accounting Standards cannot supersede the Income-tax provisions. The appellant relied on various decisions regarding the nature of meaning of interest and its allowability. The liability of interest is no doubt allowable expenditure, whereas in the present case the premium on preference shares cannot be equated with interest for the reasons mentioned above. Therefore, the various decisions relied on by the appellant cannot be applied to the present facts of the case. Thus, the argument of the appellant that the preference shares were redeemable, the premium on the redemption of the same had to be allowed as deduction u/s.36(1)(iii) of the Act cannot be accepted for the following reasons:

- a. Even though the preference shares are redeemable, it cannot be equated with the loans/borrowings. For redemption of preference shares provisions of Sec. 80 of the Companies Act, 1956 are required to be fulfilled.
- b. As per Section 80 of the Companies Act, such redemption can be made only out of the proceeds of fresh issue of shares or by creating Capital Redemption Reserve (CRR) out of the profits available for dividends. As against this for repayment of loan there is no such requirement.
- c. This CRR is treated as the paid-up share capital of the company and can be utilized only for issuing bonus shares.
- d. Such condition is laid down in order to restore the reduction in share capital caused due to redemption of preference shares.
- e. Therefore, though the preference shares are redeemable they assume nature of share capital only and not loans.

A clear distinction has been made between a loan and redeemable preference shares by the Hon'ble Calcutta High Court in the case of *Hindustan Gas and Industries Ltd.* (117 ITR 549). The Hon'ble High Court categorically held that any expenses incurred for issue for redeemable preference shares cannot be allowed as they are in the nature of capital expenditure. The Hon'ble High Court held as under in this context:

"On consideration of the provisions of the Companies Act, 1956 the contention of the assessee that when a company issues

redeemable preference shares it is in fact obtaining a loan as it could be by issuing debentures cannot be accepted. There is a fundamental difference between the capital made available to a company by issue of a share and money obtained by a company under a loan or a debenture. Respective incidences and consequences of issuing a share and borrowing money on loan or on a debenture are different and distinctive. A debenture-holder as a creditor has a right to sue the company, whereas a shareholder has no such right. Apart from that the scheme of the Companies Act and in particular the forms and contents of its balance-sheets are extremely rigid and by reason of the specific compartments in such accounts it is not possible to convert an item of capital into an item of loan as has been suggested on behalf of the assessee. In the instant case, it is the assessee who is claiming a relief or advantage by way of an allowable deduction in respect of an expenditure incurred by it. Therefore, it is strictly for the assessee to establish that the expenditure in respect of which deduction is being claimed is not an expenditure in the nature of a capital expenditure and the assessee cannot claim any benefit of ambiguity or doubt in its favour. Hence the legal charges incurred on the issue of a prospectus, underwriting commission and brokerage paid for the issue of redeemable preference shares are not revenue expenditure.”

As the above decision clearly applies to the facts of the present case, the appellant’s claim is not acceptable and the action of the A.O. is confirmed. Therefore, the ground of appeal raised by the appellant in this regard is dismissed and the A.O. is directed accordingly.”

6. *Accordingly, Ground No.2 raised by the assessee is dismissed.”*

7. Before us, assessee has not pointed out any distinguishing feature in the facts of the present case and those of earlier years. We therefore find no reason to interfere with the order of Ld.CIT(A). **Thus, the ground of the assessee is dismissed.**

8. Ground Nos.2 to 4 are with respect to disallowance of interest. Since the grounds are inter-connected, all the grounds are considered together.

9. Ground No.2 is with respect to disallowance of Rs.17,00,630/-.

9.1. During the course of assessment proceedings, AO noticed that a flat at Walkeshwar, Mumbai was taken from Atul Jain and other family members of Jain for the Officer's transit Hostel for which a total deposit of Rs.9.60 crores was paid by assessee upto 15.02.2008 to various family members of Mr Jain. He noted that the flat was used by Mr. Anil Jain as director's residence and that no rent was paid by the assessee. He also noted that none of the family members had shown any income from the aforesaid flat and no perquisite was shown by Mr. Anil Jain. The assessee was asked to justify the payments to which assessee inter-alia submitted that the flat was taken on leave and licence basis and was used by the assessee for its officers, associates. It was submitted that assessee had given interest free deposits in earlier years and during the year additional deposit was given which was commensurate with the higher valuation of the flat and that deposit was not increased since 1995. It was submitted that since interest free deposit was given in lieu of rent, assessee had claimed notional interest @ 5.50% p.a. (i.e. average cost of funds for the year under consideration) as eligible business expenses. The submissions of the assessee were not found acceptable to the AO. AO noted that assessee had borrowed funds and in majority of cases, the rate of interest was over 12%. According to the AO, had the assessee not given interest free deposits to the various persons of Jain family, the assessee would not have required to borrow loan at higher interest rate. He also concluded that the deposit paid to Director's and family was not on account of commercial expediency but was on account of favour to them. He thereafter worked out the excess interest at Rs. 17,00,630/- and disallowed the same.

10. Ground No.3 is with respect to disallowance of Rs.10,20,000/-.

10.1. AO noted that assessee had taken premises belonging to Jain Bros. Industries (deposit of Rs. 80 lacs) and Drip and Pipe suppliers (deposit of Rs.20 lacs) on rental basis against the interest free deposits given to them. AO was of the view that the reasonable deposit to the aforesaid parties was Rs.10 lacs and Rs.5 lacs respectively and thus the aggregate balance deposit of Rs.85 lacs was unreasonable. On such deposit of Rs.85 lacs, which was considered as unreasonable, he worked out the excess interest @ 12% to be unreasonable and accordingly disallowed Rs.10,20,000/-.

11. Ground No.4 is with respect to disallowance of Rs.28,87,625/-

11.1. AO noted that assessee had taken premises belonging to the directors / relatives of directors on rental basis for which assessee had given interest free deposits. The rent was adjusted against the deposits. AO was of the view that assessee had given excess deposits. He thereafter worked out the excess deposits paid to the various persons as under :

Shri B.H.Jain	Rs.3,06,00,000/-	Rs.1,81,90,317/-
Shri Ajit Jain	Rs.1,82,40,000/-	Rs.1,38,82,886/-
Shri Ashok Jain	Rs.1,14,60,000/-	Rs.79,75,029/-
Smt Nisha Jain	Rs.1,20,00,000/-	Rs.82,78,224/-
	Rs.7,23,00,000/-	Rs.4,82,36,456/-

On the excess deposit of Rs.2,40,63,544/- (Rs.7,23,00,000/- - Rs.4,82,36,456/-) as worked out by him, he worked out the disallowance of interest @ 12% and accordingly disallowed Rs.28,87,625/- as being unreasonable. Aggrieved by the order of AO, assessee carried the matter before Ld.CIT(A), who after considering the remand report and assessee's reply to the remand report, granted partial relief by observing as under:

12. With respect to disallowance of interest of Rs.17,00,630/- Ld.CIT(A) noted as under :

“4.5.2 I have carefully gone through the facts of the case. The appellant has failed to prove any nexus between the interest free funds and the interest free advances or security deposits. Moreover, the appellant had taken huge loans from banks on which it is required to pay margin money. Hence, appellant's contention suggesting that its interest free funds/own funds were kept aside and the interest free loans/security deposits were given out of these kept aside funds is devoid of merit. A perusal of Audit report for AY. 2008-09 reveals that the appellant company has taken total secured loans and unsecured loans at Rs. 907.04 crore in AY. 2008-09 as against Rs. 739.73 crore in AY. 2007-08. Schedule 19 of the Audit report reveals that the appellant company had debited Rs. 83.77 crore in P & L account on account of interest and finance charges (excluding interest received at Rs. 3.04 crore). Besides, the appellant company has debited Rs. 29.63 crore on account of discounting charges, bank. commission and charges. Taking into consideration the above stated figures, the cost of borrowing comes at 12.50%. As against this the AO has disallowed interest @ 12% on interest free loans/security deposits given by the appellant to it related concerns and directors. The appellant's calculation of cost of borrowing @ 5.3% is therefore, found contrary to the facts given above. There is no doubt whatsoever, that the appellant has used borrowed funds for non-business purposes and hence claim of interest on those funds u/s 36(1)(iii) is not tenable. The Hon'ble ITAT Hyderabad in the case of Ravindra Singh Arora Vs. ACIT (2012) 53 SOT 124 (Hyderabad) in regard to disallowance of interest u/s 36(1)(iii) has held as under :

37. Section 36(1)(iii) of the Act provides for deductions of interest

on the loans raised for business purposes. Once the assessee claims any such deduction in the books of accounts, the onus will be on the assessee to satisfy the Assessing Officer that whatever loans were raised by the assessee, the same were used for business purposes. If in the process of examination of genuineness of such a deduction, it transpires that the assessee had advanced certain funds to sister concerns or any other person without any interest, there would be very heavy onus on the assessee to be discharged before the Assessing Officer to the effect that in spite of pending term loans and working capital loans on which the assessee is incurring liability to pay interest, there was justification to advance loans to sister concerns for non-business purposes without any interest and accordingly, the assessee should be allowed deduction of interest being paid on the loans raised by it to that extent. 38. The entire money in a business entity comes in a common kitty. Monies received as

38. The entire money in a business entity comes in a common kitty. Monies received as share capital, as term loan, as working capital loan or as sale proceeds do not have any different colour. Whatever are the receipts in the business, that have the colour of business receipts and have no separate identification. Sources has no concern whatsoever. The only thing sufficient to disallow the interest paid on the borrowing to the extent the amount is lent to sister concern without carrying any interest for non-business purposes would be that the assessee has some loans or other interest bearing debts to be repaid. In case the assessee had some surplus amount which, according to it, could not be repaid prematurely to any financial institution, still the same is either required to be circulated and utilised for the purpose of business or to be invested in a manner in which it generates income and not that it is diverted towards sister concern free of interest. This would result in not presenting true and correct picture of the accounts of the assessee as at the cost being incurred by the assessee, the sister concern would be enjoying the benefits thereof. It cannot possibly be held that the funds to the extent diverted to sister concerns or other persons free of interest were required by the assessee for the purpose of its business and loans to that extent were required to be raised. We do not subscribe to the theory of direct nexus of the funds between borrowings of the funds and diversion thereof for non-business purposes. Rather, there should be nexus of use of borrowed funds for the purpose of business to claim deduction under Section 36(1)(iii) of the Act. That being the position, there is no escape from the finding that interest being paid by the assessee to the extent the amounts are diverted to sister concern on interest free basis are to be disallowed.

39. If the plea of the assessee is accepted that the interest free advances made to the sister concerns for non-business purposes was out of its own funds in the form of capital introduced in business, that again will show a camouflage by the assessee as at the time of raising of loan, the assessee will show the figures of capital introduced by it as a margin for loans being raised and after the loans are raised, when substantial amount is diverted to sister concerns for non-business purposes without interest, a plea is sought to be raised that the amount advanced was out of its capital, which in fact stood exhausted in setting up of the unit.

Such a plea may be acceptable at a stage when no loans had been raised by the assessee at the time of disbursement of funds. This would depend on facts of each case.

40. Once it is borne out from the record that the assessee had borrowed certain funds on which liability to pay tax is being incurred and on the other hand, certain amounts had been advanced to sister concerns or others without carrying any interest and without any business purpose, the interest to the extent the advance had been made without carrying any interest is to be disallowed under Section 36(1)(iii) of the Act.”

On the facts and in the circumstances of the case and keeping in mind the judicial view on the subject, in my opinion there was a justification for the disallowance out of interest paid, considering large interest free deposits, given to the owners of the flats. In the facts and circumstances of the case, I am of the view that AO was justified in disallowing interest of Rs.17,00,630/-. The same is confirmed.”

13. With respect to disallowance of interest of Rs.10,20,000/-

Ld.CIT(A) noted as under:

“4.9.1 I have perused the records/details filed and submissions made. The issue of company's own funds or deposits out of interest free fund, has already discussed in para 4.5 above. There is absolutely no doubt that while on the one hand company has borrowed funds from banks/FIs, on the other hand it is giving huge, disproportionate funds in the name of security deposits to its related concerns and directors. This way the appellant company has diverted borrowed funds for non-business purpose. A perusal of Audit report for A.Y. 2008-09 reveals that the appellant company has taken total secured loans and unsecured loans at Rs. 907.04 crore in A.Y. 2008-09 as against Rs. 739.73 crore in A.Y. 2007-08. Schedule 19 of the Audit report reveals that the appellant company had debited Rs. 83.77 crore in P & L account on account of interest and finance charges (excluding interest received at Rs. 3.04 crore). Besides, the appellant company has debited Rs. 29.63 crore on account of discounting charges, bank commission and charges. Taking into consideration the above stated figures, the cost of borrowing comes at 12.50%. As against this the AO has disallowed interest @ 12% on interest free loans/security deposits given by the appellant to its related concerns and directors. The appellant's calculation of cost of borrowing @ 5.3% is found contrary to the facts given above. In the facts and circumstances of the case, I am of the view that AO was justified in disallowing interest of Rs.10,20,000/-. The same is confirmed.

14. With respect to disallowance of interest of Rs.28,87,625/-

Ld.CIT(A) noted as under:

“4.10.1 Here also the company had taken land on hire from Shri. B. H. Jain and bungalow from other directors (related parties) for which interest free deposits had given more than 10/12 years back. In addition, rent was also payable which is being adjusted against the said deposits. The appellant has made the same arguments as made against the disallowance of interest of Rs.10,20,000 referred to in the preceding paras. The identical issue has been discussed in detail in para 4.5 and 4.9 above. The facts are identical. The AO has calculated interest at 12% on the amount of estimated excess deposit of Rs. 40,63,544/- and worked out the disallowance out of interest paid at Rs. 28,87,625/-. Keeping in view my decision in para 4.5 and 4.9 in regard to rate of interest i.e. @ 12% the addition of Rs. 28.87.625/- is confirmed.”

Aggrieved by the order of Ld.CIT(A), assessee is now in appeal before us.

15. Before us, Ld.AR reiterated the submissions made before lower authorities and further submitted that no disallowance on account of excessive interest was made in earlier years even though the substantial deposits were given by assessee in earlier years. In support of the aforesaid contention that no disallowance was made in earlier years, he placed on record the copy of the assessments framed u/s 143(3) of the Act for AY 2006-07 and AY 2007-08. He further submitted that the assessee has sufficient interest free deposits in the form of Share capital and free Reserves which are far in excess of the amount of deposits given by the assessee. He pointed to the copy of the Balance Sheet placed at page 71 of the Paper Book and pointed to the figure of shareholders fund of Rs.965.10 crores. He therefore submitted that when the shareholders funds are far in excess of the deposits given, then it is presumed that the amount of deposits given are out of interest free funds and for this proposition, he relied on the decision of Bombay High Court in the case of CIT Vs. Reliance Utilities and Power Ltd., reported in 313 ITR 340 (Bom). He also placed

reliance on the decision of Pune Tribunal in the case of Trinity India Limited in ITA No.666/PN/2012 order dt.28.08.2013. He therefore submitted that no disallowance of interest on notional basis is called for in the present case and therefore the addition made by the AO be deleted. Ld DR on the other hand took us through the order of AO and Ld.CIT(A) and supported the order of lower authorities.

16. We have heard the rival submissions and perused the material on record. The issue in the present grounds is with respect to disallowance of interest by holding that the deposits paid to the respective parties are excessive. It is an undisputed fact that in most of the cases, the deposits have been given by the assessee to the various parties in earlier years and during the year under consideration to some of the parties, further deposits have been given. It is also an undisputed fact that in the assessments framed u/s 143(3) of the Act for AY 2006-07 and 2007-08, no disallowance of the interest on account of the deposits being excessive and unreasonable was made by the AO. The total deposit given by the assessee upto the year, as per the details as given on page 134 of the Paper Book is Rs.13.26 crore as against which the availability of interest free funds in the form of Share capital and Reserves and Surplus as at the end of the financial year 31st March 2008 is in excess of Rs.965 crores indicating that the availability of interest free funds with the assessee to be far in excess of the amounts given on deposits. When the availability of interest free funds are far in excess of the amounts given as deposits, then as per the decision of Hon'ble Bombay High Court in the case of Reliance Utilities (supra), a presumption arises that the deposits are

out of interest free funds and no interest bearing funds are utilized for making the deposits. The ratio of the aforesaid decision of Hon'ble Bombay High Court in the case of Reliance Utilities (supra) has been followed by the various benches of Pune Tribunal. Before us, Revenue has not brought on record any contrary binding decision in its support. We therefore following the ratio of the aforesaid decision rendered in the case of Reliance Utilities (supra) hold that in the present case, no disallowance of interest is called for. **Thus, the grounds of the assessee are allowed.**

17. Ground No.5 is with respect to disallowance of depreciation on non compete fees.

17.1. Assessee had claimed depreciation of Rs.18,28,125/- on WDV of non compete fee of Rs.73,12,500/- treating the same as intangible asset. Ld.CIT(A) in para 4.12.1 of the order has noted that no view on depreciation was taken by the AO in the assessment order. Ld.CIT(A), relying on the decision of Hon'ble Delhi High Court in the case of Sharp Business System Vs. CIT (ITA No.492 of 2012 and C.M. Appeal No.14836 of 2012) held that non-compete fee is neither revenue expenditure nor intangible asset and therefore does not qualify for depreciation u/s 32(1)(ii) of the Act. He accordingly following the aforesaid decision of the Hon'ble Delhi High Court denied the claim of depreciation. Aggrieved by the order of Ld.CIT(A), assessee is now in appeal before us.

18. Before us, Ld.A.R. reiterated the submissions made before AO and Ld.CIT(A). He further submitted that assessee had claimed deduction of Rs.1,30,00,000/- on account of non compete fee in A.Y. 2006-07. The claim was denied by AO. When the matter was carried before Ld.CIT(A), he confirmed the order of AO but however granted depreciation by treating it as capital asset and included it block of assets and allowed depreciation at 25%. Accordingly depreciation of Rs.32,50,000/- was allowed to the assessee in A.Y. 2006-07 by Ld.CIT(A). He submitted that in subsequent year i.e., A.Y.2007-08 AO had allowed depreciation of Rs.24,37,500/- on WDV of Rs.97,50,000/- but in appellate proceedings, Ld.CIT(A) by following the decision of Hon'ble Delhi High Court in the case of Sharp Business Systems (supra) held that non-compete fees was neither revenue expenditure nor an intangible asset and therefore not entitled to depreciation u/s 32(1)(iii) of the Act. Ld.CIT(A) therefore after giving enhancement notice, denied the claim of depreciation of Rs.24,37,500/-. Aggrieved by the order of Ld.CIT(A), assessee carried the matter before ITAT. The Co-ordinate Bench of the Tribunal vide order dated 09.06.2017, decided the issue in favour of assessee. He therefore submitted that once an asset has entered in a block of asset, it loses its identity and has taken the shape of depreciable asset and thereafter the block of asset cannot be disturbed and the claim of depreciation on the WDV cannot be denied. He therefore relying on the decision of Co-ordinate Bench of the Tribunal, submitted that the claim of assessee of allowing depreciation be allowed. Ld.D.R. on the other hand, supported the order of lower authorities.

19. We have heard the rival submissions and perused the material on record. The issue in the present ground is with respect to allowing depreciation on intangible assets. It is an undisputed fact that the claim of depreciation was allowed to the assessee in A.Y. 2006-07 and the intangible assets had entered into block of assets in A.Y. 2006-07. In A.Y. 2007-08, the claim of depreciation was disallowed by Ld.CIT(A). When the matter was carried before the Co-ordinate Bench of the Tribunal, the issue was decided in favour of assessee by the Co-ordinate Bench of the Tribunal by observing as under :

“36. Second issue is relating to withdrawal of depreciation on non-compete fee. Ld. Counsel for the assessee narrated the facts that the assessee allowed the payment of non-compete fee (in short ‘NCF’) as allowable Revenue expenditure. In the earlier assessment year, 2006-07, the Revenue authorities allowed the same and treated the same as Capital asset, However, they included the same in the block of assets and allowed depreciation. Thus this part of non-compete has taken a shape of depreciable asset which is duly included in the block of assets in the current Assessment Year 2007-08. However, during the assessment proceedings in the year under consideration, the assessing authorities continued to allow the depreciation in the lines of decision in Assessment Year 2006-07. However, during the First Appellate proceedings by which time the Delhi High Court has passed judgment in the case of Sharp Business System Vs. CIT vide ITA No.492/2012 & C.M. Appl. No.14836/2012 order dated 05-11-2012 has inter alia held that non-compete fee is neither a Revenue expenditure nor an intangible asset. Therefore, it does not qualify for depreciation u/s.32(1)(ii) of the Act. Hence, after giving enhancement notice the CIT(A) enhanced the assessed income by Rs.24,37,500/- and denied the claim of depreciation on the said non-compete fee. As per the discussion given in Para 5.3 and the reasons given therein the CIT(A) held that the non-compete fee is neither allowable expenditure nor depreciable asset eligible for depreciation claimed u/s.32(1)(ii) of the Act.

37. Aggrieved with the same, the assessee is in appeal with the said issue before us.

38. At the outset, Ld. Counsel for the assessee submitted that there are divergent decisions from 2 different High Courts, i.e. Delhi and Madras High Courts on the same issue. Considering the judgment in the case of CIT Vs. M/s. Vegetable Products 88 ITR 192 (SC) the judgment which is in favour of the assessee is required to be considered, i.e., the judgment in the case of Madras High Court in the facts of the present case. Further, elaborating the facts, Ld. Counsel for the assessee submitted that this is a case of second year of claim of depreciation. AO is not allowed to take out this depreciable asset out of the block of assets created in the Assessment Year 2006-07, Relying on

the Pune Bench decision in the case of Finolex Cables Limited Vs. DCIT and vice versa in ITA Nos. 360 and 564 & 565/PN/2014 order dated 31-08-2015 Ld. Counsel for the assessee submitted that Revenue authorities are prevented restructuring the plot for any reasons of decisions. Bringing our attention to contents of Para Nos. 11 to 13 the assessee is found eligible for claim of depreciation on the written down value of the intangible asset in the impugned assessment year. For the sake of completeness of this order, we proceed to extract the said paragraphs as under :

“11. We have heard the submissions of rival sides at length and have examined the orders of the authorities below. As far as the facts are concerned, the Revenue has not raised any dispute. The only point of contention is; Whether the assessee is eligible to claim depreciation on the payment of lumpsum amount paid by assessee to Shin Etsu for the supply of raw material (preform) at the reduced rate? It is an undisputed fact that the lumpsum payment of 285 million Japanese Yen was made by the assessee in the period relevant to assessment year 2004-05 and the assessee had capitalized the same in the very first year itself. The assessee had claimed depreciation on the said amount in the assessment years 2004-05, 2005-06 and 2006-07. The Revenue had accepted the claim of assessee in each of the said assessment years. In the impugned assessment year, the Assessing Officer disallowed the claim on the ground that no capital asset was acquired by the assessee. No intangible asset, like technical knowhow, had come into existence, therefore, the assessee cannot claim depreciation on the payments made to Shin Etsu. In the first appeal, the Commissioner of Income Tax (Appeals) rejected the claim of assessee with following observations:

“14. I have carefully considered the facts of the case as well as reply of the appellant, in this case, undisputed fact remains that the amount in question has been paid in respect of raw material which could not be obtained by the appellant on account of delay in setup of plant. The appellant due to crash in prices and in order to keep the business relationship agreed to pay on account of unsupplied quantity of preforms and claims the same to be intangible asset by way of commercial right. This claim of the appellant is without any merit as no right has been acquired by the appellant and the same was paid merely to keep the purchase agreement alive and reduce the prices of preforms. Therefore, I do not find any infirmity in the order of Assessing Officer, The claim of the appellant that the amount was part of WDV brought down from earlier years is also unsustainable as wrongly brought down WDV cannot be accepted as sacrosanct. Therefore, I do not find any merit in the ground taken and therefore, the same is dismissed.”

12. The assessee in the period relevant to assessment year 2004-05 had capitalized the amount of 285 million Japanese Yen and had claimed depreciation thereon year after year. This fact is evident from the balance sheet filed by the assessee for the financial year ending on 31-03-2004, 31-03-2005 and 31-03-2006. Once, it has become the part of block of asset on which the depreciation has been allowed for the three assessment years, the depreciation cannot be denied in the subsequent assessment years on the written down value. The asset cannot be taken out of block of assets. Similar view has been taken by the Tribunal in the case of Kodak Polychrome Graphics (I) (P) Ltd. Vs. ACIT (supra). The relevant extract of the findings of the Tribunal on the issue of disallowance of claim of depreciation is as under:

“20. We have considered the rival contentions, perused the relevant findings of the Assessing Officer as well as the learned Commissioner (Appeals) and the material placed on record. It has not been disputed before us that the assets on which the depreciation has been claimed in this year are forming part of block of assets and the written down value on such assets is coming from the earlier years. On such assets, depreciation has been allowed by the Department in the assessment year 2000-01 and 2002-03 and also in the subsequent assessment years. Once the depreciation has been allowed on "Block of Assets", the same cannot be disallowed in this year on the written down value. Thus, without going into the aspects as to whether marketing data base and facility for use of network and human resources are in the nature of business or commercial rights of similar nature in the nature of intangible assets within the meaning of section 32(1)(ii), we set aside the impugned order passed by the learned Commissioner (Appeals) and direct the Assessing Officer to allow the depreciation on such assets as it has been allowed in the earlier year and is part of "block of assets". Consequently, ground no.4, raised by the assessee is treated as allowed.”

13. Thus, in view of the facts of the case, we are of the considered view that the assessee is eligible to claim depreciation on the written down value of intangible assets in the impugned assessment year. The appeal of the assessee is allowed, accordingly.”

39. From the above contents, it is settled principle that the claim of depreciation needs to be allowed on the written down value of the intangible asset. Segregation of a depreciable asset out of block of assets is not permitted artificially. Denial of asset specific depreciation out of such block of assets is also not permitted. The said judgment of Delhi High Court in the case of Sharp Business System (Supra) was decided prior to the decision of the Tribunal. Therefore, we are of the view that Ground No.2 should be allowed in favour of the assessee in view of judgment of Apex Court in the case of Vegetable Products (supra).

20. Before us, no change in facts has be pointed out by Revenue. We therefore following the order of Co-ordinate Bench of the Tribunal in assessee's own case for A.Y. 2007-08 hold that assessee is eligible for depreciation. **Therefore, the ground is allowed.**

21. **In the result, the appeal of assessee is partly allowed.**

Order pronounced on 28th day of February, 2018.

Sd/-	Sd/-
(SUSHMA CHOWLA)	(ANIL CHATURVEDI)
न्यायिक सदस्य / JUDICIAL MEMBER	लेखा सदस्य / ACCOUNTANT MEMBER

पुणे Pune; दिनांक Dated : 28th February, 2018.

Yamini

आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent
3. CIT(A)-II, Nashik.
4. CIT-II, Nashik.
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, "बी" / DR, ITAT, "B" Pune;
6. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER

// True Copy //

वरिष्ठ निजी सचिव / Sr. Private Secretary
आयकर अपीलीय अधिकरण ,पुणे / ITAT, Pune.