

**आयकर अपीलीय अधिकरण, 'ए' न्यायपीठ, चेन्नई**  
**IN THE INCOME TAX APPELLATE TRIBUNAL, 'A' BENCH, CHENNAI**  
**श्री एन.आर.एस. गणेशन, न्यायिक सदस्य एवं ए. मोहन अलंकामणी, लेखा सदस्य के समक्ष**  
**BEFORE SHRI N.R.S. GANESAN, JUDICIAL MEMBER AND**  
**SHRI A.MOHAN ALANKAMONY, ACCOUNTANT MEMBER**

**आयकर अपीलसं./I.T.A.Nos.1526 to 1528/CHNY/2014**

(निर्धारणवर्ष / Assessment Years: 2008-09, 2009-10, 2010-11)

The Deputy Commissioner of Income Tax, Large Taxpayer Unit – II, Chennai.	Vs	M/s. Rane Brake Lining Ltd., 32, Cathedral Road, Chennai – 600 086.
		PAN: AAACR1703L
(अपीलार्थी/Appellant)		(प्रत्यर्थी/Respondent)

**&**

**आयकर अपीलसं./I.T.A.Nos.1593 to 1596/CHNY/2014**

(निर्धारणवर्ष / Assessment Years: 1999-2000, 2001-02, 2006-07 & 2007-08)

M/s. Rane Brake Linings Ltd., (now known as Rane Brake Lining Limited) Plot No.30, Industrial Estate, Ambattur, Chennai – 600 058.	Vs	The Deputy Commissioner of Income Tax, Large Taxpayer Unit – II, Chennai.
PAN: AAACR1703L		
(अपीलार्थी/Appellant)		(प्रत्यर्थी/Respondent)

निर्धारिती की ओर से /Assessee by	:	Shri S. Bharath, CIT
राजस्व की ओर से /Revenue by	:	Shri R. Vijayaraghavan, Advocate

सुनवाई की तारीख /Date of hearing	:	11.01.2018
घोषणा की तारीख /Date of Pronouncement	:	15.02.2018

**आदेश / ORDER**

**Per A. Mohan Alankamony, AM:-**

The Revenue has raised three appeals against the orders of the Ld. Commissioner of Income Tax (Appeals), Large Taxpayer Unit, Chennai all dated 20.02.2014 in ITA Tr No.19/13-14/LTU(A), ITA No.95/11-12/LTU(A) & ITA 27/12-13/LTU(A) for

the assessment years 2008-09, 2009-10 & 2010-11 respectively passed U/s.143(3) of the Act.

2. The assessee has also raised four appeals against the orders of the Ld. Commissioner of Income Tax(Appeals), Large Taxpayer Unit, Chennai all dated 20.02.2014 in ITA Tr No.33/10-11/LTU(A) passed U/s.250(6) r.w.s. 143(3) & 147 of the Act for the assessment year 1999-2000, ITA Tr No.16/10-11/LTU(A) passed U/s.250(6) r.w.s. 143(3) & 254 of the Act for the assessment year 2001-02, ITA Tr.No.15/10-11/LTU(A) passed U/s.250(6) r.w.s. 143(3) of the Act for the assessment year 2006-07 and ITA Tr.No.18/10-11/LTU(A) passed U/s.250(6) r.w.s. 143(3) of the Act for the assessment year 2007-08.

3. **Revenue's Appeal:-**

The Revenue has raised several identical grounds in its appeals for the assessment years 2008-09, 2009-10 & 2010-11 and they are briefly stated hereunder for adjudication:-

- (i) The Ld.CIT(A) has erred in deleting the disallowance made by the Ld.AO amounting to Rs.18,14,642/-, Rs.19,45,374/- & Rs.26,71,000/- for the assessment years 2008-09, 2009-10 & 2010-11 respectively invoking the

provisions of U/s.40(a)(i) of the Act towards non-deduction of tax at source on the payment made for export commission to non-resident for services rendered outside India.

- (ii) The Ld.CIT(A) has erred in deleting the disallowance of Rs.16,70,142/- & Rs.3,63,415/- for the assessment year 2008-09 & 2009-10 respectively U/s.40(a)(ia) of the Act towards payment made for software licenses without deducting tax at source
- (iii) The Ld.CIT(A) has erred in deleting the disallowance made by the Ld.AO towards provision made for future loss on the unsettled Forex derivatives amounting to Rs.8,15,000/- for the assessment year 2010-11.

4. **Assessee's Appeal:-**

The assessee has raised several identical grounds in its appeals for the assessment year 1999-2000,2001-02,2006-07 & 2007-08 and they are briefly stated hereunder for adjudication:-

- i. The Ld.CIT(A) has erred in confirming the order of the Ld.AO who had disallowed proportionate interest incurred for non-business purposes amounting to Rs.1,38,22,871/- (Rs.1,35,21,690 + Rs.3,01,181) for the assessment year

1999-2000 and Rs.2,58,95,828/- (5999696 + 19896132)  
for the assessment year 2001-02.

- ii. The Ld.CIT(A) has erred in confirming the order of the Ld.AO who had disallowed 5% of dividend income towards expenditure attributable for earning exempt income invoking the provisions of Section 14A of the Act amounting to Rs.14,89,815/- & Rs.43,15,240/- for the assessment years 2006-07 & 2007-08 respectively.

**Revenue's Appeal:**

5. **Ground No. 3(i) :Disallowance of export commission payments made to non-resident agents invoking Section 40(a)(ia) of the Act for the assessment years 2008-09,2009-10 & 2010-11:-**

During the course of scrutiny assessment proceedings, it was observed by the Ld.AO that the assessee had paid commission to agents outside India. On query it was explained by the assessee that the commission payments to non-resident agents made outside India was towards export contracts procured abroad. However the Ld.AO was of the opinion that the assessee

had incurred expenses which amounts to fees for technical services whereby provisions of Section 9(1)(vii) of the Act would apply. Therefore the Ld.AO invoking the provisions of Section 40(a)(ia) of the Act disallowed the commission payments made outside India to foreign agents for all the above three assessment years.

5.1 On appeal the Ld.CIT(A) for all the three assessment years mentioned herein above, after analyzing the nature of payments made to various parties directed the Ld.AO to delete the disallowances made U/s.40(a)(ia) of the Act with respect to commission paid to foreign agents for services rendered outside India and with respect to certain other payments sustained the addition since the requisite particulars were not provided before him.

5.2 At the outset, we do not find any infirmity in the order of the Ld.CIT(A) on this issue because it has been decided by the Hon'ble Jurisdictional Madras High Court in the case CIT vs. Faizon Shoes Pvt. Ltd., reported in 367 ITR 0155 that payment made to foreign agents for services rendered outside India, tax need not be deducted at source because with respect to foreign

agents income does not accrue or arise in India for services rendered outside India. Following the ratio laid down by the Hon'ble Jurisdictional Madras High Court the Ld.CIT(A) has rightly granted relief to the assessee wherever he could arrive at the conclusion that the commission payments were made to foreign agents for services rendered outside India and in other instances, he has sustained the addition because the assessee was unable to furnish any particulars before him. Accordingly the orders of the Ld.CIT(A) is confirmed for all the three assessment years 2008-09, 2009-10 & 2010-11.

**6. Ground No.3(ii) : Disallowance of expenditure towards software license for the assessment years 2008-09 & 2009-10:-**

During the course of scrutiny assessment it was observed by the Ld.AO that the assessee had made payments towards purchase of software license for both the assessment years. For the assessment year 2008-09, the license was with respect to purchase of 21 Nos. of SAP licenses from M/s. Rane Holdings Ltd, Autocad 2007 software license and purchase of up gradation R&D software from Apana Technologies, Chennai. Since the assessee had not deducted tax at source towards the payment

made for using the software, the Ld.AO invoked the provisions of Section 40(a)(ia) of the Act.

6.1 On appeal for the assessment year 2008-09, the Ld.CIT(A) deleted the disallowance because in the case of SAP license, Autocad and R&D upgradation software were 'off the shelf' software which are in the nature of copy-righted article and not a copy-right. Payment made to certain other software's pertaining to Research & Development, the Ld.CIT(A) did not adjudicate the issue because the Ld.AO had already allowed the claim of the assessee vide his rectification order dated 25.03.2013 for the assessment year 2008-09. The Ld.CIT(A) had further allowed the appeal of the assessee for the assessment year 2009-10 for the same reasons.

6.2 At the outset, we find merit in the order of the Ld.CIT(A). When the software is purchased 'off the shelf' for usage as a product, provisions of Section 40(a)(ia) of the Act would not be applicable because it is not a payment made for any service rendered. Therefore the Ld.CIT(A) has rightly decided the issue in favour of the assessee. Therefore in this situation we do not find it

necessary to interfere with the orders of the Ld.CIT(A) for both the assessment years 2008-09 & 2009-10 on this issue.

**7. Ground No. 3(iii) : Disallowance of the provision made for future loss on the unsettled Forex derivatives amounting to Rs.8,15,000/- for the assessment year 2010-11**

During the course of scrutiny assessment proceedings it was observed by the Ld.AO that the assessee had claimed loss due to exchange fluctuation amounting to Rs.8,15,000/- on the unsettled forex derivatives. On query it was explained by the assessee that to mitigate the risk of loss due to foreign exchange transaction the company has taken forward cover with respect to its debtors and creditors. It was further explained that on valuing the debtors and creditors as on 31.03.2010, with respect to the foreign exchange transactions, the loss was arrived at Rs.8,15,000/-. However the Ld.AO taking cue from Section 43(5)(d) of the Act arrived at the conclusion that the derivative transaction which is not settled by actual delivery has to be treated as speculative transaction and therefore not allowable as deduction. The Ld.AO was further of the view that the loss debited to the P&L account by restating their receivables / payables with the prevailing exchange rate as on 31.03.2010 is only a provision

created for unascertained liability and therefore not allowable as deduction under the Income Tax Act.

7.1 On appeal the Ld.CIT(A) granted relief to the assessee by observing as follows:-

*“I have carefully considered the facts of the case and the submissions of the ld.AR. As per the decision of Hon'ble Supreme Court in the case of Woodward Governors India P Ltd, 312 ITR 254 (2009) (SC) and several other cases, the foreign exchange fluctuation loss was allowed as business loss. It was also recognized the forward contracts as hedging tools to protect the interest of the business from the volatility of the foreign currency. The precondition for allowing such losses are the followance of guidelines of RBI and FEMA and the Forward Contracts (FCs) should be within the value of the invoices. The foreign exchange loss / gain at the end of the closure of the accounts ie., 31<sup>st</sup> March was also permitted as per the Accounting Standards. However, as per the decision in the case of London Star Diamond Company (I) P.Ltd in ITA No.6169/M/2012 dated 11.10.2013 A.Y.09-10, the ITAT Mumbai has held that the appellant should furnish the satisfactory explanation to the AO if the forward contracts were closed prematurely if the loss needs to be allowed. The loss incurred by the appellant appears to be the loss due to the closure of accounts as on 31<sup>st</sup> March, in which case the loss incurred on Mark to Market basis as on 31<sup>st</sup> March needs to be allowed. I direct the AO accordingly. The ground is allowed.”*

7.2 On analyzing the facts of the issue, we find merit in the order of the Ld.CIT(A). The assessee has arrived at the value of its receivables and payables as on the end of the relevant previous year with respect to foreign exchange transactions resulting from trading activity and such loss due to the fluctuation in foreign currency falls in the revenue field. Moreover, as per the

Accounting Standards such loss has to be recognized in the end of the relevant previous year in which such loss has incurred. The Ld.CIT(A) has rightly relying on the decision of the Hon'ble Apex Court and the other decisions cited in his order and also taking note of the Accounting Standards has allowed the appeal of the assessee. In this situation, we do not find it necessary to interfere in his order.

### **Assessee's Appeal**

**8. Ground No.4(i) : Disallowance of proportionate interest incurred for non-business purposes amounting to Rs.1,38,22,871/- (Rs.1,35,21,690 + Rs.3,01,181) for the assessment year 1999-2000 and Rs.2,58,95,828/- for the assessment year 2001-02:-**

In both the above mentioned relevant assessment years, it was observed by the Ld.AO that the assessee had made investment in sister concerns from its interest bearing funds. Therefore the Ld.AO relying on the decision of the Tribunal disallowed the interest attributable with respect to such investment and thereby made addition for the assessment year 2001-02 amounting to Rs.2,58,95,828/- (interest of Rs.59,99,696/- towards current year investment in shares and interest of Rs.1,98,96,132/-

towards investment in shares made in earlier years). Similarly additions were made for the assessment year 1999-2000 for Rs.1,38,22,871/-.

8.1 On appeal the Ld.CIT(A) upheld the order of the Ld.AO for the assessment year 1999-2000 by observing as follows:

*“6.2 I have carefully considered the facts of the case and the submissions of the Id.AR. I have also gone through the decisions relied on by the Id.AR and AO. The AO has observed that the loans were advanced from O.D. Alc of ICICI Bank. The appellant has argued that it has sufficient own funds and the amounts advanced were from internal accruals. It has submitted that all the own funds and the borrowed funds were also mingled in common account. Therefore, the Id.AR has argued that the AO is not correct in stating that the loans advanced to sister concerns were only from O.D. alc and the consequent disallowance of proportionate interest is protested. With regard to the subject of disallowance of deemed interest, two things need to be seen –*

*(i) whether the borrowed funds were used for the business purpose for which they were borrowed and entire interest debited is only for the business activity of the assessee. [ CIT v. Calcutta Agency Ltd, 19 ITR 191 (SC) ]*

*(ii) whether the loans advanced to sister concerns are out of commercial expediency [ S.A. Builders Ltd v. CIT, 288 ITR 1 (SC) ],*

*6.2.1 In the instant case, it is made very clear by the AO that the loans advanced to the sister concerns have a direct nexus with their O.O. funds borrowed from the ICICI bank. Therefore, the interest burden directly fell on the appellant and the entire interest debited in its account was not meant for the business activity of the appellant. The appellant also submitted in its written submissions dated 15.3.2012 as under:*

*"Para 3.2..... The loans borrowed for the purpose of business were credited to the common account where both borrowings as well as profits and other non- interest bearing funds which were mingled together. It cannot therefore be said with certainty that the investments were*

made only out of borrowings and not out of profits embedded in the account."

*It goes without saying that the advances to the sister concerns have gone from a common fund which includes interest free own funds and interest bearing borrowed funds. Even though the appellant has contended that linking up of O.D. funds to diversion of funds to sister concerns is not proper, but at the same time it could not establish with certainty and cogent evidence that only the interest free own funds have-been diverted to sister concerns. Further, the onus is on the appellant to prove that all the expenses, including interest, debited in the P&L are meant for the business of the appellant. In the instant case, the appellant has failed to prove that the entire expenditure of interest debited in P&L are for the loans borrowed and used for its own business. In view of the above discussion, the appellant has failed the first test that the entire interest expenditure debited in its account was only related to earning of its business income.*

*6.2.2 With regard to other test whether funds diverted to sister concerns was out of commercial expediency or not, no evidence was filed either before the AO or before me to show that the funds given to the sister concerns were out of necessity of the appellant's business. There is no gain in any way to the appellant out of the funds diverted to the sister concerns. No evidence of whatsoever was filed before me to show that the sister concerns were sick or in dire need of money and a revival is needed to help run the appellant business smoothly. There was no evidence filed before me that the sister concern do not have independent sources of funds to run their business. Since they also belong to Rane group of companies and having reputation they themselves could have approached the banks and obtain loans on their own. The Id.AR has not produced any of such evidences except stating as under in its written submissions.*

"3.1 ... Out of the retained earnings, the appellant made strategic investments in group companies viz., Rane(Madras) Ltd, Rane LUK Clutch Ltd, JMA Range Marketing Ltd. The group companies are part of 'Rane' group which deals in the manufacture of automobile ancillaries. Thus, the investment in the group was in the course of business activity as the investee companies are also in the auto ancillary industry."

*From the above, it is clear that there is no commercial expediency to divert the interest bearing or any loans to the sister concerns at its own*

*cost. The simple rhetoric, that the "strategic investments" were made in the group companies since they are also into auto ancillary industry, is not a sound argument. I also agree with the argument of the AO that had the funds were not diverted to sister concerns, the appellant company would not have approached the banks for loans or have gone for a lesser borrowings and the interest burden would have been less on the appellant. It is also pertinent to note the observation of the AO that the free funds were locked up in other assets like fixed assets, current assets etc.*

*6.2.3 In view of the above discussion, I am of the opinion that the funds were not given out of any commercial expediency and the disallowance of deemed interest @ 12% made by the AO is in order. The ground is dismissed."*

For the assessment year 2001-02 also, the Ld.CIT(A) following his order for the assessment year 1999-2000 upheld the view of the Ld.AO.

8.2 At the outset we do not find any infirmity in the orders of the Ld.Revenue Authorities on this issue. It is evident from the facts of the case that the assessee has invested its interest bearing funds in equity shares earning dividend income which is exempt from tax. Moreover nothing is brought out before us to establish that these investments are made for strategy purposes or due to commercial exigencies. Obviously expenses incurred towards investment made for earning exempt income cannot be charged to the business operations of the assessee, because such expenditure are not related to the business of the assessee.

The assessee as well as its sister concerns are different entities as per the provisions of the Act and only the expenses that are incurred by the assessee towards its respective business activities will be allowable as deduction. Therefore we are of the considered view that the decision of the Ld.Revenue Authorities on this issue is appropriate. Hence we do not find it necessary to interfere in their orders on this issue.

**9. Ground No. 4(ii) : Disallowance U/s.14A of the Act for Rs.14,89,815/- & Rs.43,15,240/- for the assessment years 2006-07 & 2007-08 respectively:-**

During the course of scrutiny assessment for the assessment year 2006-07, it was observed by the Ld.AO that the assessee has utilized its borrowed funds towards advancing loan to subsidy company M/s. Rane Dye Cast Limited amounting to Rs.1,12,45,000/- and has also purchased 28,60,000 shares of M/s. Rane Dye Cast Limited for Rs.5,84,87,000/-. Thus the assessee had diverted Rs.6,97,32,000/- for non-business purposes. With respect to the amount of interest bearing funds advanced to M/s.Rane Dye Cast Limited for Rs.1,12,45,000/- in the assessment year 2006-07, the Ld.AO disallowed the amount of Rs.31,86,608/- being the amount of interest attributable towards

the same because it was not incurred for the business of the assessee.

9.1 On appeal the Ld.CIT(A) confirmed the order of the Ld.AO by observing as under:

*“5.2 I have carefully considered the facts of the case and the submissions of the ld.AR. On similar issue which came up for consideration before me for A.Ys 99-2000 and 2001-02 in appellant’s own case, wherein after detailed discussion, I opined that the funds were not given out of any commercial expediency and the disallowance of deemed interest disallowance made by the AO was upheld vide my orders of even dated. Following the same, the ground is dismissed for this year also.”*

9.2 We do not find any infirmity in the order of the Ld.CIT(A) on this issue because we have upheld the order of the Ld.Revenue Authorities for the earlier assessment years herein above on the very same issue in para 8.2.

9.3 With respect to the investment on shares in M/s. Rane Dye Cast Limited for Rs.5,84,87,000/- during the assessment year 2006-07 by the assessee, it was observed by the Ld.AO that the assessee had earned dividend income of Rs.2,97,96,510/-. The Ld.AO invoking the provisions of Section 14A of the Act disallowed 5% of the same which works to Rs.14,89,815/-. On

appeal the Ld.CIT(A) confirmed the order of the Ld.AO by observing as follows:

*7.2 I have carefully considered the facts of the case and the submissions of the Id.AR. Similar issue was decided by me in appellant's own case for A.Y.2002-03 wherein the disallowance made by the AO of 2% was confirmed, keeping in view the facts and circumstances of the case for that year. For this assessment year 2006-07, the AO has deemed it fit to disallow 5% of the gross dividend income as expenditure relatable to exempt income. Since the ITAT, Chennai in the case of Celebrity Fashions in ITA NO.1318 and 1319/Mds/2011 for A.Ys 2006-07 & 2007-08 has found 5% of the gross dividend received as reasonable. Respectfully following the above decision, I confirm the disallowance made by the AO. In view of this, the other points raised on this issue by the appellant deemed to have been answered. The ground is dismissed.”*

9.4 On the similar issue Hon'ble Jurisdictional High Court in the case M/s. Simpson & Co. Ltd vs. DCIT in Tax case (Appeal) No.2621 of 2006 dated 15.10.2012 has held that 2% of dividend income may be disallowed for the purpose of compliance U/s.14A of the Act which was followed by the Tribunal in the case DCIT vs. M/s. Data Software Research Company (P) Ltd in ITA Nos.1837 & 1838/Mds/2014 vide order dated 17.07.2015 at para No.17. Therefore following the decision of the Hon'ble Jurisdictional Madras High Court and the decision of the Chennai Bench of the Tribunal supra, we hereby direct the Ld.AO to disallow 2% of the dividend income which works out to Rs.5,95,930/-.

9.5 With respect to the disallowance U/s.14A of the Act for the assessment year 2007-08 the Ld.AO has disallowed 5% of the dividend income invoking Section 14A of the Act. On the identical issue with respect to the other appeal of the assessee discussed herein above we have held that 2% of dividend income may be disallowed following the decision of the Hon'ble Jurisdictional Hon'ble Madras High Court in the case M/s. Simpson & Co. Ltd., and the decision of the Chennai Bench of the Tribunal cited supra. Therefore for the assessment year 2007-08 also the same decision holds good because Rule 8D of the Rules is not applicable for the relevant assessment years.

10. In the result the Revenue's appeal in ITA Nos.1526, 1527 & 1528 of 2014 are dismissed and the Assessee's appeal in ITA Nos. 1593 & 1594 of 2014 are dismissed and in ITA Nos. 1595 & 1596 of 2014 are partly allowed.

Order pronounced on the 15<sup>th</sup> February, 2018 at Chennai.

Sd/-

(एन.आर.एस. गणेशन)  
(N.R.S. Ganesan)

न्यायिक सदस्य/Judicial Member

Sd/-

(ए. मोहन अलंकामणी)  
(A. Mohan Alankamony)

लेखा सदस्य/Accountant Member

चेन्नई/Chennai,

दिनांक/Dated 15<sup>th</sup> February, 2018

**RSR**

आदेश की प्रतिलिपि अग्रेषित/Copy to:

- |                        |                          |                              |
|------------------------|--------------------------|------------------------------|
| 1. अपीलार्थी/Appellant | 2. प्रत्यर्थी/Respondent | 3. आयकर आयुक्त (अपील)/CIT(A) |
| 4. आयकर आयुक्त/CIT     | 5. विभागीय प्रतिनिधि/DR  | 6. गार्ड फाईल/GF             |