

**IN THE INCOME TAX APPELLATE TRIBUNAL  
HYDERABAD BENCH 'B', HYDERABAD**

**BEFORE SMT. P. MADHAVI DEVI, JUDICIAL MEMBER  
AND SHRI S. RIFAUR RAHMAN, ACCOUNTANT MEMBER**

ITA No. 65/Hyd/2017  
Assessment Year: 2012-13

RA Chem Pharma Ltd., vs. Income Tax Officer,  
Hyderabad. Ward – 3(2), Hyderabad.

PAN – AAACI 6448M

Appellant

Respondent

ITA Nos. 48 & 49/Hyd/2017  
Assessment Year: 2010-11 & 2012-13

Dy. Commissioner of vs. RA Chem Pharma Ltd.,  
Income-tax, Circle – 3(1), Hyderabad.  
Hyderabad.

PAN – AAACI 6448M  
Respondent

Appellant

Assessee by: Shri S. Rama Rao  
Revenue by: Shri R. Mohan Reddy

Date of hearing: 04/06/2018  
Date of pronouncement: 08/06/2018

**ORDER**

**PER S. RIFAUR RAHMAN, AM:**

ITA Nos. 65/Hyd/2017 and 49/Hyd/2017 are cross appeals filed by the assessee as well as revenue and ITA No. 48/Hyd/2017 filed by the revenue for AY 2010-11. As identical issues are involved in these appeals, they were clubbed and heard together and therefore we find it convenient to pass a consolidated order.

ITA No. 65/Hyd/2017 by the assessee for AY 2012-13

2. In this appeal, the assessee has raised the following grounds of appeal:

1. *Unexplained Investments - Discrepancy in Purchases - Rs 22646910/-*

*The impugned order has erroneously sustained the addition of Rs 226.46 lacs as unexplained investments on account of difference between the statement of purchases submitted at the time of assessment and the purchases in the Final Accounts.*

2. *Unexplained Investments - Discrepancy in creditor balances - Rs 28396925/-*

*The impugned order has sustained the addition of 283.96 Lacs being the difference between the creditors' statements and the creditors balance as per the Final Accounts as unexplained investments without considering that these arose on account of post dated cheques.*

3. *Notional Interest on loan to wholly owned subsidiary - Rs 1463729*

*The company gave an interest free loan of Rs 121.97 lacs to its wholly owned subsidiary Indu Pharma Ltd. The LD AO disallowed a notional interest expenditure of Rs 14.63 lacs which has been erroneously sustained by in the impugned order*

4. *HP Interest - R 34204/-*

*The company incurred hire purchase interest expenditure of Rs 34204/- from Reliance Capital which is not liable to TDS deduction.*

5. *TDS deducted at lower rate- Rs 2123400*

*The impugned order has erroneously disallowed proportionate expenditure on X - Ray Charges Rs 3.01 lacs) and Screening Charges (Rs 1822 lacs) on the*

*ground that it has not met with TDS at the applicable rates. Your appellant submits that the lower deduction of TDS does not call for a proportionate disallowance of expenditure.*

*In view of the above facts and circumstances, your appellant prays that this appeal be allowed and the order of the Hon'ble CIT (Appeals) be set aside."*

3. Briefly the facts of the case are, the assessee is engaged in the business of bulk drugs and clinical research activities. It filed return of income on 29/09/2012, declaring income of Rs. 21,53,61,060/- . Scrutiny assessment was passed u/s 143(3) on 17/03/2015 determining the assessed income under the normal provisions at Rs. 27,48,76,726/- by making various additions.

4. Against the assessment order, the assessee preferred an appeal before the CIT(A) and the CIT(A) passed an ex-parte order deciding the appeal based on the information available on record when the assessee failed to appear before him even though the number of opportunities provided. Aggrieved, the assessee is in appeal before us.

5. We dispose of the appeal ground-wise as under:

6. As regards ground No. 1 pertaining to the addition of Rs. 2,26,46,910/- towards discrepancy in purchases, the AO observed that as per the inventory, the purchases were Rs. 95,37,45,924/-, whereas, as per P&L Account, the purchases were Rs. 93,10,99,014/-, therefore, the investment in excess purchases of Rs. 2,26,46,910/- was treated as unexplained investment rejecting the explanation of the assessee that the difference between the figures was on account of other costs that are also accounted as part of purchase cost such as Freight, inward, customs duties, loading etc.

6.1 The CIT(A) confirmed the action of the AO by holding that though in grounds of appeal of the assessee claimed that difference in purchases is due to freight, inward, customs duty, loading, unloading etc., the relevant details of such payments are not available on record, they do not form part of P&L A/c also and, therefore, assessee failed to reconcile the figures.

6.2 Before us, the Id. AR submitted a reconciliation statement which is part of paper book (refer page 179). He brought to our notice that AO has not considered the expenses relating to imports and inter unit transactions. He prayed that this may be considered.

6.3 The Id. DR relied on the assessment order.

6.4 Considered the rival submissions and perused the material on record. As the assessee has submitted a reconciliation statement highlighting the difference between the purchases recorded in P&L a/c and stock register, it needs verification, therefore, we remit this issue to the file of AO to verify the claim of the assessee and consider the same after giving proper opportunity of being heard. This ground is allowed for statistical purposes.

7. As regards ground No. 2 pertaining to the addition of Rs. 2,8396,925/- towards discrepancy in creditor balances, the AO observed that the as per the list of sundry creditors submitted by the assessee, the sundry creditors were Rs. 36,85,55,847/- whereas as per the balance sheet the sundry creditors were Rs. 39,69,52,772/-. The AO, therefore considered the difference of Rs. 2,83,96,925/- as unexplained credit.

7.1 The CIT(A) confirmed the addition rejecting the submission of the assessee that the difference in sundry creditors is due to non-adjusting of post dated cheques in respective creditors balances on the ground that no such details were submitted either during assessment or during appeal proceedings.

7.2 Before us, the Id. AR submitted that the difference is due to issue of post dated cheques and the same was not represented properly before the AO and CIT(A).

7.3 The Id. DR relied on the order of AO.

7.4 Considered the rival submissions and perused the material on record. Since the assessee has not properly submitted the information before AO and not properly represented before Id. CIT(A), this issue needs to be verified by AO afresh considering additional evidence submitted before us and accordingly, we remit this issue back to AO to verify the same after giving proper opportunity of being heard to the assessee. This ground is treated as allowed for statistical purposes.

8. As regards ground No. 3, addition of Rs. 14,63,729/- towards notional interest on loan to wholly owned subsidiary, the AO observed that on perusal of balance sheet, it is revealed that the assessee company had given loans to its sister concerns from the interest bearing funds borrowed from banks. He opined that the diversion of funds to the sister concerns attracts disallowance of interest proportionate to the loan amount. He, therefore, held that as the assessee company had given a loan of Rs. 1,21,97,738/- to its sister

concern and no interest is received, the interest at 12% on Rs. 1,21,97,738/-, which comes to Rs. 14,63,792/- was disallowed from the interest claimed by the assessee.

8.1 The CIT(A) confirmed the addition by observing that though the assessee claimed that the amount was given to wholly owned subsidiaries in the course of business to protect the value of investments in subsidiaries, no details were submitted as to what are the shares held by the assessee in subsidiaries, nature of business of subsidiary companies etc.

8.2 Before us, the Id. AR submitted that assessee granted interest free advance to its wholly owned subsidiary in the course of business. It is done in the interest of the subsidiary, it amounts to investments in order to protect the share holding interest. This issue is squarely covered by the Hon'ble Supreme Court decision in the case of SA Builders.

8.3 The Id. DR relied on the order of AO.

8.4 Considered the rival submissions and perused the material on record. We notice that assessee has given advance to its wholly owned subsidiaries in the course of business. We also notice that assessee has huge reserves at its disposal to the extent of Rs. 48.99 crores and also employed borrowed funds. When the assessee has huge reserves in its disposal and diverts Rs. 1.22 crores to its wholly owned subsidiaries, the AO cannot link the transaction with the borrowed funds. The wholly owned subsidiaries are the extension of the assessee company. It can divert funds to its subsidiary to protect the interest of the shareholding. It is in line with the ratio laid down in the case of SA Builders

(supra) even it can divert the borrowed funds. For the sake of clarity, it is reproduced as under:

*“We wish to make it clear that it is not our opinion that in every case interest on borrowed loan has to be allowed if the assessee advances it to a sister concern. It all depends on the facts and circumstances of the respective case. For instance, if the Directors of the sister concern utilize the amount advanced to it by the assessee for their personal benefit, obviously it cannot be said that such money was advanced as a measure of commercial expediency. However, money can be said to be advanced to a sister concern for commercial expediency in many other circumstances (which need not be enumerated here). However, where it is obvious that a holding company has a deep interest in its subsidiary, and hence if the holding company advances borrowed money to a subsidiary and the same is used by the subsidiary for some business purposes, the assessee would, in our opinion, ordinarily be entitled to deduction of interest on its borrowed loans.”*

Respectfully, following the said ratio, we delete the disallowance of Rs. 14,63,792/- made by the AO towards interest.

9. As regards ground No. 4 pertaining to the addition of Rs. 34,204/- on account of hire purchase interest expenditure, the AO disallowed the said amount being the payment made to Reliance capital on the ground that no TDS was deducted.

9.1 The CIT(A) confirmed the addition on the ground that there was no evidence on record regarding the nature of transaction to verify whether the same is liable to TDS or not.

9.2 Before us, the Id. AR submitted that it is hire purchase interest which is not liable to TDS deduction.

9.3 The Id. DR relied on the orders of revenue authorities.

9.4 Considered the rival submissions and perused the material on record. We notice that assessee has made

payment to Reliance Capital and not deducted TDS and it claims that it is relating to hire purchase transaction, for which TDS provision will not apply. We notice that there is no much discussion about this issue in assessment order, again this needs verification. We direct the AO to verify the same and if it is found that it is hire purchase transaction, which is exempt as per CBDT Instruction No. 1425, dated 16/11/1981. Therefore, it may be allowed. This ground is allowed for statistical purposes.

10. As regards the addition of Rs. 21,23,400/- pertaining to TDS deduction at lower rate, the AO disallowed the said amount on the ground that the assessee has not met with TDS at the applicable rates.

10.1 The CIT(A) confirmed the addition.

10.2 Before us, the Id. AR submitted that AO invoked section 40(a)(ia) erroneously on the ground that such expenses were met with TDS at a lower rate instead of at the applicable rate.

10.3 The Id. DR relied on the order of AO.

10.4 Considered the rival submissions and perused the material on record. We notice that AO has disallowed the expenditure by observing that assessee has deducted tax on part of amount of expenses claimed and again he observes that assessee will not be treated as TDS complied when tax deducted at source partly and at irrelevant rate or in applicable rate. At the same time, Id. CIT(A) observes that as per information on record, it is not the case of short deduction of TDS, it is the case of not deducting TDS on some payment. Again this also needs verification and if it is short deduction,

AO cannot invoke section 40(a)(ia) and further, assessee is not held to be assessee in default. In case it is found that it is the case of non-compliance with the TDS provision, AO may be justified with his action. Accordingly, the issue is remitted to the file of the AO. This ground is allowed for statistical purposes.

Appeals by the revenue for AY 2010-11 and 2012-13

11. In these two appeals, the revenue has raised the following grounds of appeal, which are common in both the appeals under consideration:

*“1. The Ld. CIT (A) erred both in law and on facts of the case.*

*2. The Ld. CIT (A) erred in deleting the disallowance of amortization of expenditure claimed of Rs.33,85,779/-*

*3. The Ld. CIT (A) erred in not considering the fact brought on record by the Assessing Officer that the assessee is not eligible for claim of deduction either through amortization of expenditure or by way of claiming depreciation.*

*4. The Ld. CIT (A) ought to have considered the fact that the expenditure claimed by the assessee was not incurred in the relevant previous year and does not fall in the ambit of provisions of section 35D or 35DD.*

*5. Any other ground(s) that may be urged at the time of hearing.”*

12. The brief facts of the case as taken from AY 2010-11, are that the assessee incurred an expenditure of Rs. 129.85 lakhs during AY 2007-08 and 2008-09 towards research and development and began amortising the same from AY 2009-10 onwards @ 20% per annum. Inventis Drug Delivery System Pvt. Ld. was merged with the assessee company during FY 2008-09 relevant to AY 2009-10 and this company incurred an amount of Rs. 39.43 lakhs towards product development

expenditure during AY 2005-06 & 2006-07 and started amortising the expenditure @ 10% from AY 2007-08 onwards. Both the combined expenses were amortized by the assessee and claimed the same as under:

S.No.	AY	Amount claimed	% of amortization	Name of the company
1	2007-08	394357	10%	Inventis
2	2008-09	394357	10%	Inventis
3	2009-10	4174494	20%(*)	Assessee
4	2010-11	3385779	20% of Rs. 16928893 (Rs. 12985327 + 3943566)	Assessee company

(\*) 20% of Rs. 1,29,85,327/- = Rs. 25,97,065

20% of Rs. 39,43,566/- = Rs. 7,88,713/-

10% of Rs. 39,43,566/- = Rs. 3,94,356/-

(As inventis claimed only 10% in AY 2007-08 the balance 10% is claimed now)

10% of Rs. 39,43,566/- = Rs. 3,94,356/-

(As inventis claimed only 10% in AY 2008-09 the balance 10% is claimed now)

Total = Rs. 41,74,494/-

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12.1 The AO disallowed the amortization expenses of Rs. 35,89,413/- on the following reasons:

*a) Sec. 35D refers to amortization of preliminary expenses and section 35DD refers to amortization of expenses in case of amalgamation or demerger. Whereas in the instant case the amortised expenditure was incurred towards research and development therefore the same cannot be allowed either under Sec.350 or 3500.*

*(b) The expenditure does not pertain to the previous year 2009-10, therefore the same cannot be allowed U/s 35(1) or U/s 37.*

*(c) Alternative claim of the assessee that the expenditure resulted in an intangible asset and depreciation should be allowed u/s 32 is also rejected as no such claim was made in earlier years.*

13. On appeal, before the CIT(A), the assessee submitted as under:

*(a) The amortization of expenses in assessee's own case for A. Y .2009-10 was allowed by Assessing Officer in scrutiny assessment u/s 143(3) dated 29.12.2011.*

*(b) Similarly amortization of expenses claimed in Inventis for A.Y.2006-07 (u/s.143(3) dated 18.12.2008) & 2007-08 ( u/s.143(3) dated 31.12.2009) were also allowed.*

*(c) The expenses incurred for research and development resulted in knowhow which enhanced the profit earning capacity resulting in enduring benefit, therefore such expenditure is capital in nature and depreciation should be allowed. Reliance is placed on Larsen and Toubro Vs CIT (2012) Taxpub (DT) 2928 J K synthetics (1994) 207 ITR 985*

*(d) The same expenditure was allowed in earlier year, consistent treatment should be adopted by the Assessing Officer. Reliance is placed on Radha Soami Satsang Vs CIT (1992) 193 ITR 321 ( SC)*

*(e) The deferred revenue expenditure was held allowable in the following cases.*

*Madras Industrial Investment Corp. ( 1997) 225 ITR 802 ( SC)*

*Taparia Tools (2015) 327 ITR 605*

*CIT Vs Sanco Trans Ltd (2006) 284 ITR 51 ( Madras)*

14. The CIT(A) after considering the submissions of the assessee, directed the AO to allow the deferred revenue expenditure of Rs. 33,85,779/- by observing as under:

*6. The information on record is carefully considered. The appellant incurred the expenses towards research and development as mentioned at Para (3).the claim made in P&L account is Rs. 35,89,413 and not Rs. 33,85,779. The Assessing Officer did not doubt the genuineness of*

*the expenditure. The Assessing Officer observed that the expenditure is not allowable u/s 32/35(1)/ 35D/35DD /37 for the reasons mentioned at Para (4). The appellant incurred the expenses and according to him the result of such expenses shall accrue over a period of five years. Accordingly he has been claiming the expenses @20%. Though there is no concept of deferred revenue expenditure in Income Tax Act, 1961, the same is well accepted accounting principle as held by the Hon'ble Supreme Court in case of Madras Industrial Investment Corporation wherein the Hon'ble Supreme Court held that "although the assessee has incurred the liability to pay the discount in the year of issue of debentures, the payment was to secure a benefit over a number of years. There is continuing benefit to the business of the company over the entire period and hence the expenditure was allowed to the claim or spread over the period of the debentures.*

*Further in the case of Radha Soami Satsang VS CIT ( cited supra ) the Hon'ble Supreme Court observed that "In the absence of any material change justifying the Department to take a different view from that taken in earlier proceedings, the question of the exemption of the assessee appellant should not have been reopened. Strictly speaking, res Judicata does not apply to IncomeTax proceedings. Though, each assessment year being a unit, what was decided in one year might not apply in the following year; where a fundamental aspect permeating through the different assessment years has been found as a fact one way or the other and parties have allowed that position to be sustained by not challenging the order, it would not be at all appropriate to allow the position to be changed in a subsequent year."*

*Therefore this expenditure to be allowed fully in the year of incurring or alternatively on deffered basis over a period of time. Keeping in view the principle of consistency the Assessing Officer is directed to allow deferred revenue expenditure of Rs. 33,85,779. Since the first ground of appeal is allowed, the alternative ground of appeal regarding allowing depreciation becomes infructuous and treated as dismissed."*

15. Aggrieved by the order of CIT(A), the revenue is in appeal before us.

16. Ld. DR submitted that the claim of the assessee is not proper as the expenses are not in revenue in nature and also assessee has not proved that it is in capital expenditure. In both counts, it cannot be allowed as allowable expenditure. Accordingly, he relied on the assessment order.

17. Ld. AR submitted that these expenses are revenue expenditures and brought to our notice the details of expenses, which is placed on record at page 123 of paper book. He submitted that AO is not disputing the fact that it is R&D expenditure and AO analysed this issue in the light of section 35D & 35DD. The assessee never claimed the deduction u/s 35D or 35DD. It is deferred revenue expenditure, which is allowable as expenditure by relying on Madras Industrial Investment (supra) case.

18. Considered the rival submissions and perused the material on record. As submitted before us, the assessee has incurred R&D expenses and on evaluation, it was found that it has enduring benefit spread over to next five years. Accordingly, claimed deduction @ 20%. It is not the case of AO that the expenses were not incurred but whether it is allowable as expenditure u/s 35D or 35DD or can it be allowed as capital expenditure to qualify for deduction u/s 32. Even though, assessee has not represented properly before Id. CIT(A), but, the Id. CIT(A) has analysed the issue in light of decisions in the case of Madras Industrial Investment (supra) and Radha Soami Satsang (supra) and came to the conclusion that it is allowable expenditure. Considering the overall facts of the matter, the conclusion drawn by the Id. CIT(A) is proper, particularly, on the matter of consistency. Therefore, ground raised by the revenue is accordingly rejected.

19. In the result, assessee's appeal in ITA No. 65/Hyd/2017 is allowed for statistical purposes and revenue appeals in ITA Nos. 48 & 49/hyd/2017 are dismissed.

Pronounced in the open court on 8<sup>th</sup> June, 2018.

Sd/-  
(P. MADHAVI DEVI)  
JUDICIAL MEMBER

Sd/-  
(S. RIFAUR RAHMAN)  
ACCOUNTANT MEMBER

Hyderabad, dated 8<sup>th</sup> June, 2018

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Copy forwarded to:

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4. CIT(A) - 3, Hyderabad
5. Pr. CIT - 3, Hyderabad
6. The DR, ITAT, Hyderabad
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