IN THE INCOME TAX APPELLATE TRIBUNAL, DELHI 'B' BENCH, NEW DELHI

BEFORE SHRI N.K. BILLAIYA, ACCOUNTANT MEMBER, AND SHRI K.N. CHARY, JUDICIAL MEMBER

ITA No. 3185/DEL/2016
[Assessment Year: 2011-12]

The A.C.I.T. Circle 8(1) Delhi	Vs.	Eichers Motors Ltd 3rd Floor, Select CityWalk A-3, District Centre Saket, New Delhi PAN: AAACE 3882 D
[Appellant]		[Respondent]

Date of Hearing : 14.05.2019
Date of Pronouncement : 16.05.2019

Assessee by : Shri Gaurav Jain, Adv.
Ms. Deepika Agarwal, Adv
Shri Arpit Goyal, CA

Revenue by : Ms. Nidhi Srivastava, CIT, DR

ORDER

PER N.K. BILLAIYA, ACCOUNTANT MEMBER,

This appeal by the Revenue is preferred against the order of the Commissioner of Income Tax [Appeals]-XIII, New Delhi dated 22.03.2016 pertaining to assessment year 2011-12.

2. The grievance raised by the Revenue is two-fold:

(i) the Revenue is aggrieved by the deletion of addition of Rs. 7.60 crores made by the Assessing Officer on account of excess deduction claimed by the assessee u/s 35(2AB) of the Income-tax Act, 1961 [hereinafter referred to as 'the Act']; and,

(ii) the revenue is aggrieved by the deletion of addition of Rs. 3.92 crores made by the Assessing Officer on account of provision for warranty.

3. Facts relating to Ground No. 1 are that during the course of scrutiny assessment proceedings, the Assessing Officer noticed that the assessee has claimed deduction of Rs. 8,83,57,145/- on account of Research & Development expenditure u/s 35/35(2AB) of the Act. The Assessing Officer found that the said deduction has been claimed @ 150% of the total expenses claimed to be incurred under nomenclature weighted deduction.

4. The assessee was asked to justify its claim. The assessee filed a detailed reply vide submission dated 22.11.2013. The detailed submission in relation to the claim of weighted deduction did not find any favour with the Assessing Officer. The Assessing Officer proceeded by disallowing excess claim of deduction of Rs. 7.60 crores. The operative part of the assessment order reads as under:

> "After the perusal of the assessee's submissions it has been found that the assessee has claimed additional deduction u/s 35(2AB) on the R&D activities done by it. The deduction allowable u/s 35(2AB) of the IT Act requires certain conditions. These conditions have been enumerated in rule 7A of the IT rule which says that:-
>
> Approval of expenditure incurred on in house R&D facility by company under subsection (2AB) of section 35 shall be subject to the following conditions, namely:-
>
> a) The facility should not relate purely to market research sales promotion, quality control, testing commercial production, style changes, routine data collection or activities of a like nature.

b) The prescribed authority shall submit its report in relation to the approval of in- house Research and Development facility in Form No. 3CL to the Director General (Income Tax Exemptions) within sixty days of its granting approval,

c) The company shall maintain a separate account for each approved facility, which shall be audited annually and a copy thereof shall be furnished to the Secretary, Department of Scientific and Industrial Research by 31[sl] day of October of each succeeding year.

Explanation: For the purposes of this sub-rule the expression [1] audited" means the audit of accounts by an accountant, as defined in the Explanation below sub-section (2) of section 288 of the Income Tax Act, 1961.

d) Assets acquired in respect of development of scientific research and development facility shall not be disposed of without the approval of the Secretary, Department of Scientific and Industrial Research.

Therefore, the Income tax Rule provides for complete set of conditions which needs to be fulfill in totality for the claim of deduction u/s 35(2AB). In the instant case the assessee fulfill the conditions of rule 7A(b),(c),d) but the conditions stated in rules 7A (a) is not fulfilled. Here it is pertinent to note that as stated by assessee itself that the main objective of

their R&D program are meeting customer needs, innovating and adopting technology improvements to excite customers, upgrade and modified I products, focus towards environments. The assessee has developed products like classic style vehicle for export, cruiser type vehicle for domestic market, variant of electra in F.Y. 2008-09. Whereas similar products in F.Y 2009-10 and 2010-11 as well. These products have been developed by the assessee for the sole purpose of increasing their business profits in terms of sales. Therefore, the entire purpose of the inclusion of provisions of additional deduction u/s 35(2AB) in the statutes get defeated. Rule 7 A (a) clearly states that the facility should not relate purely to market research, *sale promotions, quality control, testing, commercial production, style changes etc.* This provision has been included in Income Tax Act to give boost to the scientific research' in the country which will eventually lead to larger benefit of the society and nation.

However, the assessee here is doing R&D purely for the purpose of increasing their sales by producing items that can be sold in domestic or overseas markets by bringing in changes in style, design or technology to invite more customers.

In view of the above discussion the additional deduction u/s 35(2AB) I.T. Act, claimed by the assessee amounting to Rs. 7,60,64,206/- is being disallowed.

Accordingly .deduction for R&D is worked out as:

Deduction U/s 35 as per Tax Audit Report:	Rs. 8,83,57,145/-
Less .Allowable Capital expenditure U/s 35:	Rs. 1,22,92,939/-
Additional Weighted Deduction claimed:	Rs. 7,60,64,206"

5. Proceeding further, the Assessing Officer found that the assessee has made provision for warranty at Rs. 3.92 crores which is debited in the profit and loss account. The assessee was asked to furnish the basis to compute the provisional amount and also asked to explain as to why the same should not be disallowed, being the expenses relating to unascertained liability and provisional in nature.

6. On receiving no plausible reply, the Assessing Officer was of the opinion that such provisions cannot be allowed and disallowed Rs. 3.92 crores.

7. Aggrieved by these two additions, the assessee carried the matter before the CIT(A) and reiterated its claim of weighted deduction and provision for warranty.

8. The CIT(A), after considering the facts and submissions was convinced with the claim of the assessee and deleted the additions.

9. Before us, the ld. DR strongly supported the findings of the AO.

10. The ld. AR stated that the issue relating to claim of weighted deduction has been decided by the Tribunal in assessee's own case in A.Ys 2009-10 and 2010-11 by the Hon'ble High Court and the co-ordinate bench.

11. We have given a thoughtful consideration to the orders of the authorities below. We have also gone through the decisions of the co-ordinate bench and the Hon'ble High Court of Delhi placed before us in the case law paper book from pages 2 to 29. The relevant findings of the Hon'ble High Court in ITA No. 136/2017 order dated 15.09.2017 read as under:

> "12. The Court is unable to concur with the impugned order of the ITAT on both the aspects. Having held that the R&D

expenditure as claimed by the Assessee ought to have been allowed, there was no question of remanding the matter to the AO for returning a finding on whether the expenditure was of revenue or capital nature. This is because, under Section 35 (2AB) of the Act, both revenue and capital expenditure are allowable in their entirety, excluding expenditure in the nature of cost of any land or building. There was going to be no purpose served in analysing whether the expenditure was of revenue or capital nature. In fact, the AO himself had allowed 100% of the expenditure both of revenue and capital nature and the disallowance was only the additional 50% amount which, again, the CIT (A) had found and correctly so, in the opinion of this Court, ought not to have been disallowed. Recently, this Court in W.P.(C) 9306/2015 Maruti Suzuki India Limited Vs. UOI & Anr, by its decision dated 4th August, 2017 has held "The legislative intent behind this provision is to encourage innovation, research and development in India and non-grant of the benefit under Section 35 (2AB) defeats the legislative intent." In that view of the matter, the Court has no hesitation in holding that the Assessee is entitled to the full benefit of Section 35 (2AB) and that the ITAT was in error in remanding this issue to the AO for a fresh decision".

12. The revenue preferred SLP before the Hon'ble Supreme Court and the Hon'ble Supreme Court in SLP Civil Diary No. 29548/2018 dismissed the SLP of the Revenue. Respectfully following the findings of the Hon'ble High Court of Delhi [supra] and the co-ordinate bench in ITA No. 2561/DEL/2013 read with the decision of the Hon'ble High Court of Delhi in ITA No. 136/2017, we decline to interfere with the findings of the CIT(A). Ground No. 1 is, accordingly, dismissed.

13. In so far as Ground No. 2 is concerned, we find that similar disallowances were made by the Assessing Officer in A.Ys 2003-04 to 2009-10 and in A.Y 2010-11. The disallowances were deleted by the CIT(A) and the revenue did not prefer any appeal till A.Y 2008-09. In A.Ys 2009-10 and 2010-11, dispute relating to similar disallowances travelled upto the Tribunal and the Tribunal has decided the issue in favour of the assessee and against the revenue in ITA No. 2561/DEL/2013 for A.Y 2009-10 and ITA No. 2228/DEL/2014 for A.Y 2010-11. The relevant findings of the co-ordinate bench in ITA No. 2228/DEL/2014 read as under:

"19. AO disallowed an amount of Rs.2,10,00,000/- being excess of actual warranty claimed out of Rs.3,67,00,000/- made as provision for warranty by the assessee company on the ground that it was not ascertained liability. CIT (A) vide impugned order deleted the disallowance of Rs.2,10,00,000/-.

20. The ld. AR for the assessee relied upon the order passed by coordinate Bench of the Tribunal in ITA No.2561/Del/2013 order dated 04.01.2016 for AY 2009-10 in assessee's own case and contended that there is no change of circumstances and the said 10 ITA Nos2228 & 2268/Del./2014 order has not been further challenged by the revenue. For facility of reference, Paras 31, 32 & 33 of the order (supra) are reproduced as under for ready reference :-

> *"31. Undisputedly, assessee is engaged in the business of manufacturing and sale of commercial vehicles, tractors, two wheelers and gears. Ld. A.R. contended that various products of the company are sold along with warranty and assessee is under obligation to replace any component bearing manufacturing defect free of cost and at the end of the relevant previous year, assessee had made aggregate provisions for warranty at Rs.7,38,00,000/-.*

32. Ld. D.R. relied upon the order passed by Assessing Officer. However, Ld. A.R. relied upon the order passed by L. CIT(A) and contended that the assessee only claimed regarding deduction of amount earmarked for provision for warranty, has been allowed by the Revenue during the Assessment Years 2002-03, 2003-04, 2006-07 and 2007-08 and no appeal has been filed by the Department against Ld. CIT(A)'s order. Ld. A.R. also relied upon the decision delivered by Income tax Appellate Tribunal Delhi Bench 'B', New Delhi in assessee's own case entitled DCIT Vs M/s. Eicher Motors Ltd. in I.T.A. No. 3560/Del12008 order dated 18.09.2009. Ld. A.R. also relied upon the judgment of Hon'ble Supreme Court in the case entitled Rotork Controls India Pvt. Ltd. Vs CIT, 314 ITR 62 (S.C.). The ratio of judgment (supra) is that estimated provisions for warranty are allowable for deduction. Operative part of the judgement (supra) is reproduced below for facility of reference:

> *"Held, reversing the decision of the Hon'ble High Court, that the valve actuators, manufactured by the assessee, were sophisticated goods and statistical data indicated that every year some of these were found defective; that valve actuator being a sophisticated item no customer was prepared to buy a valve actuator without a warranty. Therefore, the warranty became an integral part of*

the sale price: in other words, the warranty stood attached to the sale price of the product. In this case, the warranty provisions had to be recognized because the assessee had a present obligation as a result of past events resulting in an outflow of resources and a reliable estimate could be made of the amount of obligation. Therefore, the assessee had incurred a liability during the assessment year which was entitled to deduction under section 37 of the Income tax Act, 1961. 11 ITA Nos2228 & 2268/Del./2014 The present value of a contingent liability, like the warranty expense, if properly ascertained and discounted on accrual basis can be an item of deduction under section 37. The principle of estimation of the contingent liability is not the normal rule. It would depend on the nature of the business, the nature of sales, the nature of the product manufactured and sold and the scientific method of accounting adopted by the assessee. It would also depend upon the historical trend and upon the number of articles produced. A provision is a liability which can be measured only by using a substantial degree of estimation. A provision is recognized when: (a) an enterprise has a present obligation as a result of a past event: (h) it is probable that an outflow of resources will be required to settle the obligation, and (c) a reliable

estimate can be made of the amount of the obligation. If these conditions are not met, no provision can be recognized. The principle is that if the historical trend indicates that a large number of sophisticated goods were being manufactured in the past and the facts show that defects existed in some of ht items manufactured and sold, then provision made for warranty in respect of such sophisticated goods would be entitled to deduction from the gross receipts under section 37. " 33. The coordinate bench of Income tax Appellate Tribunal by relying upon the judgement cited as Rotork Controls India Ltd. (supra) in the assessee's own case for the Assessment Year 2002- 03 held that assessee had estimated the provisions for warranty on the basis of past history. The estimate of warranty made by the assessee on the basis of past history cannot be treated as a provision for any ascertained liability and allowed the provision for warranty as deduction. Following the law laid down by Hon'ble Supreme Court in the judgement (supra), decision of coordinate bench in the assessee's own case, we find that there is no infirmity or perversity in the findings returned by Ld. CIT(A) in allowing the ascertained liability as allowable expenditure u/s 3 7(1) of the Act. So, ground No.3 is determined in favour of the assessee." 21.

Following the order passed by the coordinate Bench in assessee's own case for AY 2009-10 (supra), by following the judgment passed by the Hon'ble Supreme Court in case of Rotork 12 ITA Nos2228 & 2268/Del./2014 Controls (supra), we find no illegality or perversity in the deletion of disallowance of Rs.2,10,00,000/- by the ld. CIT (A) vide impugned order. So, ground no.2 is determined against the revenue".

14. Respectfully following the findings of the co-ordinate bench [supra], Ground No. 2 is also dismissed.

15. In the result, the appeal filed by the Revenue in ITA No. 3185/DEL/2016 stands dismissed.

The order is pronounced in the open court on 16.05.2019.

Sd/- **sd/-**

[K.N. CHARY] **[N.K. BILLAIYA]**
JUDICIAL MEMBER **ACCOUNTANT MEMBER**

Dated: 16th May, 2019.

VL/

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR

Asst. Registrar
ITAT, New Delhi

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Date on which the approved draft comes to the Sr.PS/PS	
Date on which the fair order is placed before the Dictating Member for pronouncement	
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