IN THE INCOME TAX APPELLATE TRIBUNAL
'B' BENCH : BANGALORE

BEFORE SHRI. CHANDRA POOJARI, ACCOUNTANT MEMBER
AND
SMT. BEENA PILLAI, JUDICIAL MEMBER

ITA Nos. 1851/Bang/2017 & 2129/Bang/2018
Assessment Years : 2012-13 & 2013-14

M/s. Lemnisk Pvt. Ltd., (formerly known as 'Vizury Interactive Solutions Pvt. Ltd.), No. 135, 1st Cross, 5th Block, Koramangala, Bangalore – 560 095. PAN: AACCV8881B	**Vs.**	The Deputy Commissioner of Income Tax, Circle – 7 (1) (2), Bangalore.
APPELLANT		**RESPONDENT**

Assessee by	:	Shri K.R. Vasudevan, Advocate
Revenue by	:	Dr. Manjunath Karkihalli, CIT DR

Date of Hearing	:	02-03-2022
Date of Pronouncement	:	29-04-2022

ORDER

PER BEENA PILLAI, JUDICIAL MEMBER

Present appeals filed by assessee against the order passed by the Ld.CIT(A) dated 26/05/2017 and 27/04/2018 assessment years 2012-13 and 2013-14 respectively passed by the Ld. CIT(A)-7, Bangalore, on the following grounds of appeal:

ITA 1851/Bang/2017 (A.Y. 2012-13)

1. Disallowance of web hosting charges paid – Rs.28,14,822

a. The learned Commissioner Income Tax (Appeal)[hereinafter referred as CIT(A)] and the learned Assessing Officer (hereinafter referred as AO) have erred in disallowing web hosting charges of Rs. 28,14,822 for non-deduction of tax at source.

b. The learned CIT(A) and the AO have erred in concluding that web hosting charges paid is in the nature of fees for technical service (-FTS") under the India — USA and India - Australia Double Tax Avoidance Agreement treaty ("tax treaty").

c. The learned CIT(A) has erred in not adjudicating the fact that the web hosting services do not involve 'human intervention' and accordingly cannot be considered as fees for technical service.

d. The learned CIT(A) and the learned AO ought to have appreciated that the web hosting services also does not make available technical knowledge, skill, know how or experience to the Appellant and accordingly not subject to withholding of taxes under the tax treaty.

e. The learned CIT(A) ought to have taken cognizance of the various judicial precedents which have held that payments made towards web hosting services cannot be considered as fees for technical services.

f. The learned CIT(A) has failed to appreciate that the web hosting charges are merely standard services obtained over Internet and as such no technical inputs are provided by the service provider to the Appellant.

2. Disallowance of Provisions- Rs. 29,39,905

a. The learned CIT(A) has erred in not providing the Appellant with an opportunity of being heard on the applicability of withholding taxes on such provisions made which is against the principles of natural justice.

b. The learned CIT(A) ought to have appreciated that TDS was not applicable on the year end provisions made by the Appellant.

c. Notwithstanding and without prejudice to the above, if the provisions made are to be disallowed, the same is to be allowed as a deduction to the appellant on reversal/payment.

3. Disallowance of Subsidiary establishment expenses- Rs.1,59,450
a. The learned AO had erred in disallowing professional charges paid towards setting up a subsidiary in Australia.
b. The learned AO has erred in concluding that the expenses incurred are capital in nature.
c. The learned CIT(A) has erred in not adjudicating this ground and merely relied on the learned AO's order.
d. The learned AO ought to have appreciated that the appellant has incurred such professional charges for the purpose of its business.

4. Disallowance of Consultancy fee paid- Rs. 11,57,540
a. The learned CIT(A) and the learned AO have erred in concluding that consultancy fees paid to M/s. People Search Pte of Singapore is fees for technical service ("FTS").under the Act and India — Singapore Double Tax Avoidance Agreement treaty ("tax treaty").
b. The learned CIT(A) and the learned AO have erred in disallowing consultancy fees paid for non-deduction of tax at source.
c. The learned CIT (A) and the learned AO ought to have observed that the services received have been utilized outside India and therefore not liable to tax.
d. The learned CIT(A) and the learned AO ought to have appreciated that the expenses have been incurred for earning income from outside India and therefore not liable to tax.
e. Notwithstanding and without prejudice to the above, even if the consultancy fees is considered as Fees for technical Service, the learned CIT(A) and the learned AO have failed to appreciate that the services of M/s. People Search Pte of Singapore do not 'make available' any technical skill, knowledge, know-how or experience to the Appellant for it to be taxable under the India — Singapore tax treaty.
f. The learned CIT(A) has erred in holding that services of recruitment would fulfil the 'make available' test without assigning any reasons.
The appellant craves leave to add, alter and modify the above grounds during the course of the appeal.
For the above and any other grounds which may be raised at the time of hearing, it is prayed that the order of the Assessing officer be set aside."

ITA 2129/Bang/2018 (A.Y. 2013-14)

"1. Disallowance of software payment - Rs,10,59,229

a. The learned CIT(A) has erred in disallowing the entire payment in relation to software capitalized during the year for non-deduction of tax as against the disallowance of depreciation made by the learned AO.
b. The learned C1T (A) has erred in not giving the Appellant an opportunity of being heard while making the disallowance.
c. The learned CIT(A) has erred in not appreciating the fact that depreciation is not covered under section 40(a)(ia) of the Act.
d. The learned CIT(A) has erred in not following the jurisdictional Tribunal Ruling on the disallowance of depreciation.
e. The learned CIT(A) has erred in alleging that the Appellant had capitalized the software costs to avoid deduction of tax at source without any basis.
f. The learned CIT(A) ought to have observed that out of the total software purchase of Rs.10,59,229, invoice pertaining to Rs. 825,746 fell within the Notification No. SO 1323(E) dated 13-06-2012 issued by Central Board of Direct Taxes (`CBDT') which notifies that no deduction of tax shall be made for purchase of software from residents.

2. Disallowance of web hosting charges paid - Rs.3,24,66,717
Payment considered as Fees for Technical Services
a. The learned CIT(A) has erred in confirming disallowance of web hosting charges amounting to Rs. 3,24,66,717 for non-deduction of tax at source.
b. The learned CIT(A) has erred in confirming that web hosting charges paid is in the nature of fees for technical service("FTS") under the India USA and India - Australia Double Tax Avoidance Agreement treaty ("tax treaty").
c. The learned CIT(A) has erred in not adjudicating the fact that the web hosting services do not involve 'human intervention' and accordingly cannot be considered as fees for technical service.
d. The learned CIT(A) ought to have appreciated that the web hosting services does not make available of technical knowledge, skill, know how or experience to the company and hence not treated as fees for technical services under the tax treaty.
e. The learned CIT(A) ought to have taken cognizance of the various judicial precedents which have held that payments made towards web hosting services cannot be considered as fees for technical services.

Payment considered as Royalty

a. The learned CIT(A) erred in contending that the web-hosting charges is also royalty on the ground that the company has right to use the confidential information of the service provider.

b. The learned CIT(A) has wrongly concluded that the legal right, title to the site are assigned to the Appellant

c. The learned CIT(A) has failed to appreciate that the web hosting charges are merely standard services obtained over internet and as such no technical inputs / rights are provided by the service provider to the Appellant.

d. The learned CIT(A) ought to have taken cognizance of the various judicial precedents which have held that payments made towards web hosting services cannot be considered as royalty.

Payment considered as Service Permanent Establishment

a. The learned CIT(A) further erred in concluding that non-resident service provider has a Service Permanent Establishment in India without any basis or bringing any facts on record.

3. Disallowance of consultancy fee paid- Rs. 3,64,72,144

a. The learned CIT(A) erred in affirming the disallowance of consultancy fee paid for non-deduction of tax at source under section 40(a)(i).

b. The learned CIT(A) ought to have appreciated that the expenses have been incurred for earning income from a source outside India and therefore not liable to tax under the provisions of section 9(1)(vii) of the Act.

c. The learned CIT(A) failed -to 'appreciate that the payments made in relation to consultancy services provided by various vendors falls under Article 12 / Article 14 of the respective tax treaties as given below:

Service provider	*Amount*	*Country*	*Article reference*
Eyal Mekler	*6,11,601*	*Australia*	*Article 12 & Article 14 of India- Australia DTAA*
Nicholas King	*15,38,265*	*Australia*	*Article 12 & Article 14 of India- Australia DTAA*
Edvaldo Acir	*37,59,010*	*Brazil*	*Article 14 of India- Brazil DTAA*
Joao Paulo Pereira Corian	*5,31,513*	*Brazil*	*Article 14 of India- Brazil DTAA*
Patricia Lorenzino	*13,29,381*	*Brazil*	*Article 14 of India- Brazil DTAA*

Thiago De Andrade	*4,22,082*	*Brazil*	*Article 14 of India- Brazil DTAA*
Careerwin Executive Search	*2,42,019*	*China*	*Article 12 of India-China DTAA*
CIIC Financial Consulting Co. Ltd	*51,12,130*	*China*	*Article 12 of India-China DTAA*
Jack Wu (Cheng-Hsien WU)	*70,01,369*	*China*	*Article 12 & Article 14 of India-China DTAA*
Liann Gao (Lingyan Gao)	*15,51,128*	*China*	*Article 12 & Article 14 of India-China DTAA*
Sachin Kulkarni	*6,37,492*	*China*	*Article 12 & Article 14 of India-China DTAA*
Kwai Wing Egan Lau	*16,26,276*	*Hong Kong*	*As per section 9(1)(i) of the Act*
Dicky Hermawan	*21,78,860*	*Indonesia*	*Article 14 of India-Indonesia DTAA*
Ridho Putradi S'Gara	*4,22,381*	*Indonesia*	*Article 14 of India-Indonesia DTAA*
Micro Ad - Inc(Consultants)	*14,05,677*	*Japan*	*Article 12 of India-Japan DTAA*
Amjad Puliyali	*4,44,136*	*UAE*	*Article 14 of India-UAE DTAA*
DLA Piper UK LLP Beijing	*8,16,592*	*China*	*Article 12 of India-China DTAA*
Chester Wu (NG Whye Jhun)	*20,88,092*	*Singapore*	*Article 12 & 14 of India-Singapore DTAA*
Chua Shuqi Lydia	*18,71,963*	*Singapore*	*Article 12 & 14 of India-Singapore DTAA*
Dannie Cho Kwok Wai	*8,73,262*	*Singapore*	*Article 12 & 14 of India-Singapore DTAA*
Philip Anthony Chan	*18,42,727*	*Taiwan*	*Article 14 of India-Taipei DTAA*
Yuchi Lee	*7,94,580*	*Taiwan*	*Article 14 of India-Taipei DTAA*
Reversals	*(6,28,482)*		
Total	***3,64,72,054***		

4. Disallowance of recruitment charges- 38,75,435

a. The learned CIT(A) has erred, in confirming the disallowance of recruitment charges paid for non-deduction of tax at source Under section 40(a)(i).

b. The learned CIT(A) failed to appreciate that the payments made in relation to recruitment services provided by various vendors fails under Article 12 / Article 14 of the respective tax treaties as given below:

Service provider	*Amount*	*Country*	*Article reference*
Bank Accout China-345460452009	*59,995*	*China*	*Article 12 of India-China DTAA*
Beijing Randstad HR Services Co Ltd	*1,7 l ,148*	*China*	*Article 12 of India-China DTAA*
Big Wave Digital Pty Limited	*15,71,032*	*Australia*	*Article 12 of India-Australia DTAA*
Michael Page International	*20,73,260*	*Singapore*	*Article 12 of India-Singapore DTAA*
Total	*38,75,435*		

c. The learned CIT(A) has failed fo adjudicate how the income of non-resident have accrued in India and has summarily held that the appellant was duty bound to deduct taxes on recruitment charges.

d. The learned CIT(A) has erred in concluding that it is mandatory for an assessee to approach the tax officer for the clearance in case where the Appellant is of the belief that withholding of taxes is not required.

The appellant craves leave to add, alter and modify the above grounds during the course of the appeal.

For the above and any other grounds which may be raised at the time of hearing, it is prayed that the order of the Assessing officer be set aside."

2. Both sides submitted that, the most of the disallowances made during years under consideration, are identical on similar facts and circumstances.

We shall consider the facts for Assessment Year 2012-13.

3. Brief facts of the case are as under:

3.1 The assessee is engaged in the business of re-targeting, that is, targeting the customers, based on their movements on customers website, social media etc. It is submitted that, retargeting is an

exercise that refers to online ad placement or display ads which targets users who have interacted with assessee's customers in a specific way. It is submitted that, once a visitor enters the customers website, clicks on a product or takes a certain action that the company wants them to take, a cookie is sent to their browser and this information is used to re-target them with the ads based on the user's interaction. The assessee submitted that, the web hosting service, is a type of Internet hosting service that allows individuals and organisation to make their website accessible via the world wide web. The vendors provide with an earmarked space on the website, and allow to save data on the servers owned by the vendors. In this entire process, the assessee uses the services of various non-resident vendors whereby, the company procures hosting services, server space for posting the ads of its customers on the designated space of the vendors cloud websites.

3.2 For assessment year 2012-13, the assessee made payments amounting to ₹28,14,822/- to Amazon, Softlayer, Rackspace Hosting etc., towards the space provided on their website. The Ld.AO observed that, the assessee did not deduct TDS on the payments made. The assessee before the Ld.AO submitted that, since the services were not rendered in India, there was no need of TDS to be deducted, as no income accrued or arose in India. It was also submitted that, the recipient do not have a permanent establishment in India and therefore, the payment did not fall within the purview of, "fee for technical services", as defined under Section 9 of the Act.

3.3 The Ld.AO did not agree with the submissions of assessee and was of the opinion that, the fee paid by assessee clearly falls within the definition of technical services under the Act, as defined in Explanation 2 to section 9(1)(vii) of the Act. The Ld.AO, thus disallowed, entire payment under section 40(a)(ia) of the Act.

3.4 The Ld.AO from details filed, observed that, the assessee created provision amounting to ₹ 29,39,905/- towards advertisement charges. It was also observed that the provision created at the end of the year was reversed on the first day of the subsequent year. The Ld.AO disallowed the said provision and added back ₹ 29,39,905/- to income, as he was of the view that, since provisions are the nature of un-crystallised liability, the same are not allowable expenses in the hands of the assessee for year under consideration.

3.5 The Ld.AO further observed that, the assessee incurred ₹ 1,59,450/- as professional services, for establishment of its subsidiary in Australia. It was the view of the Ld.AO that, the assessee should have capitalized the said expenditure. The Ld.AO, thus, added the same back to the income of assessee.

3.6 The Ld.AO observed that, during the year assessee paid ₹ 11,57,540/- to M/s. People search PTE., of Singapore, for recruitment of business development head in south-east Asia. It was also observed that assessee made payments to M/s. DLA Piper UK in Beijing, towards advisory services amounting to ₹ 12,13,580/-. The Ld.AO did not agree with the submissions of the assessee, and was of the opinion that, the fee paid by the assessee falls within the definition of “fee for technical services”,

under the Act, as defined in, Explanation 2 to section 9(1)(vii) of the Act. The Ld.AO, thus disallowed the entire payment under section 40(a)(ia) of the Act.

3.7 Aggrieved by the additions made, the assessee preferred appeal before the Ld. CIT(A).

4. The Ld.CIT(A) sustained the disallowance of web hosting charges on the ground that the service provider, had, made available knowledge, expertise relating to web hosting services to the assessee. The Ld.CIT(A) however allowed certain deductions of payment made by assessee to the vendors in following countries for the following reasons:

Country	Amount	Remarks
USA	26,83,359	Sustained by CIT(A) on the grounds that it makes available technical knowledge to the Appellant.
India	7423	Allowed as below threshold limit
Australia	124,041	Allowed as necessary taxes were deducted by the Appellant.

5. In respect of disallowance of provision, the Ld.CIT(A) upheld the addition on the ground that, the liability to deduct tax arises at the time of payment or credit of any sum to any account including suspense account.

6. In respect of disallowance of the expenses incurred to establish subsidiary in Australia, the Ld.CIT(A) upheld the addition made by the Ld.AO.

7. In respect of the consultancy fee disallowed, the Ld.CIT(A), sustained the addition by holding that, the assessee was facilitated by M/s.People Search Pte., of Singapore, in decision-making by

offering the candidates to get appointed by the assessee company in which it has an expertise. As regards to payment made to M/s.DLA Piper UK LLP, China the Ld.CIT(A) observed that tax was deducted at source and evidences were produced before the Ld.AO. The Ld.CIT(A), accordingly, directed the Ld.AO to carry out due verification in respect of the documents filed by the assessee and to delete the disallowance if taxes have been deducted and paid.

Aggrieved by the additions confirmed by the Ld.CIT(A), assessee is on appeal before the *Tribunal*.

8. It is submitted that similar disallowance is made for assessment year 2013-14. Therefore common issues in both years are considered together.

9. <u>Disallowance of Web hosting charges</u>

9.1 It is submitted that this issue is raised in **Ground No.1** for **assessment year 2012-13** and **Ground No. 2** for **assessment year 2013-14**.

9.2 The revenue made disallowance under section 40(a)(ia) of the Act in respect of the amount paid to non resident for non-deduction of TDS.

9.3 The Ld.AR submitted that, as per the provisions of the Act, 'fee for technical services' is defined under *Explanation 2* to section 9 (1) (vii) of the Act to mean, "any consideration (including any lump-sum consideration) for the rendering of any managerial, technical or consultancy services." It is submitted that, in the case of the assessee, there is no human touch or intervention or involvement in providing the advertising services and it is merely

the use of standard facility of technology that provided services. It is submitted that the payments made by the assessee is towards online advertisement that cannot be treated as fee for technical services. The Ld.AR placed reliance on following decisions of this *Tribunal*:

- *Decision of Hon'ble Kolkotta Tribunal in case of ITO vs Right Florists (P.) Ltd reported in (2013) 32 taxman.com 99*
- *Decision of Hon'ble Mumbai Tribunal in case of eBay International AG vs ADIT .reported (2012) 25 taxman.com 500*

9.4 The Ld.AR, further submitted that, as per India US DTAA, FTS is taxable only when, there is, 'make available' of technical knowledge, experience, skill, know-how or process or consistent of development and transfer of technical plan or technical design. He placed reliance on the decision of *Hon'ble Karnataka High Court* in case of *CIT vs D Beers India Minerals Pvt.Ltd.,* reported *(2012) 21 taxman.com 214* and *DIT vs Sun Microsystems India Private Ltd.,* reported in *(2014) 48 taxman.com 93.*

9.5 It is the submission of the Ld.AR that, in the present case the vendors do not "make available" any technical skill, knowledge, know-how, experience etc., or technology to assessee, while providing the web hosting services as there is no human interactions.

9.6 On the contrary, the Ld.CIT.DR, placed reliance on orders passed by authorities below.

9.7 We have perused submissions advanced by both sides in light of records placed before us.

9.8 The only payment disputed by the revenue for non-deduction of TDS for assessment year 2012-13 is in respect of the payments made to following parties:

Sl.No.	Name	Amount (in Rs.)	Country
1	Adbrite Inc	113317	USA
2	Amazon Web Services	805246	USA
4	Codesion cloud services	35874	USA
6	Jespersoft	2402	USA
7	Linkedin	38524	USA
8	Max mind	13449	USA
9	Rackspace	262472	USA
10	Softlayer	1397342	USA
11	Comodo Group Inc	14733	USA
Total		2814822	

10. For assessment year 2013-14, following are the payments made to non residents in various countries that are disallowed for non deduction of taxes.

Name	Amount (Rs.)	Country
Amazon Web Services	2,14,93,011	United States of America
Atlassian Pty Ltd	8,18,103	Australia
Rackspace	7,03,346	United States of America
Softlayer	94,52,527	United States of America
Grand Total	3,24,66,717	

11. It is the contention of the revenue that, the assessee is desirous of securing access to and use of the services that allows the assessee to serve advertisement on Internet. The revenue also contends that there is no fixed payment for the services, but are dependent on the use and access of the assessee and the services

provided by the vendor's. It is further observed by the Ld.CIT(A) that the expertise of the vendor's effect the performance of the assessee and the contention of the assessee that, since these services 'make available' technology to the assessee, the payment made to these vendor's cannot be treated as 'fee for technical services', under the Indo-US DTAA. The revenue pleaced reliance on the decision of *Hon'ble Chennai Tribunal* in case of *Foster Wheeler France USA* reported in *67 taxman.com 120* and decision of *Hon'able Cochin Tribunal* in case of *US Technology Resources Pvt.Ltd. vs ACIT* reported in *39 taxman.com 23*.

12. We note that, the Ld.AO categorised the above payments for A.Y. 2012-13 to be in the nature of "fee for technical services", whereas, the Ld.CIT(A) characterises the payments to be also in the nature of 'royalties'. The Ld.CIT(A) further holds that, there is a service PE under Article 5, in India in respect of the vendor's, and the same is taxable as business income under the relevant DTAA.

13. In our view, the payment made by assessee to the vendor's can either be FTS or royalty, under relevant DTAA, or could be categorised to be business income under Article 7, in case there exists permanent establishment in India. All 3 characters cannot be attributed to the same kind of payment made by the assessee of the vendor's.

14. We have perused the decisions relied by both sides.

In our view, characterisation of payments for digital goods/services has always been a contentious issue. Sharing of data on world wide web/Internet has become an important marketing tool for the present-day business trend. As observed

herein above, there are various decisions on this aspect which are rendered based on the peculiar facts. We note that, the payees are tax residents of various countries with whom India has DTAA. Therefore, in view of Section 90(2) of the Act the provisions of the Act or the DTAA whichever is more beneficial to the assessee shall apply.

15. In our view, the conclusions with regard to payment for 'right to use' software will equally apply to these types of payments and these has to be analysed in the light of the agreements entered into between the assessee and vendors in respective countries, in the light of the principles laid down by *Hon'ble Supreme Court* in case of *Engineering Analysis Centre of Excellence Pvt.Ltd.,* reported in *(2021) 125 taxmann.com 42*, having regard to the DTAA.

16. Various decisions relied by the Ld.AR as well as, the Ld.CIT.DR are based on the facts therein, however the basic principle enunciated by *Hon'able Supreme Court* in case of *Engineering Analysis Centre of Excellence Pvt.Ltd.(supra),* that domestic law cannot override the treaty benefits, cannot be ignored.

17. *We* therefore remand this issue back to the Ld.AO for *de novo* verification, in order to correctly characterise the nature of payment made by the assessee to various vendors. It may also be noted that, treaty benefits available to assessee cannot be done away with, in case it the circumstances so warrant.

Accordingly Ground No.1 for assessment 2012-13 and Ground No.2 for assessment year 2013-14 stands allowed for statistical purposes.

18. <u>Disallowance of consultancy fees paid by assessee to various nonresidents:</u> This issue is raised by the assessee in **Ground No.4** for assessment in 2012-13 and **Ground No.3** for assessment year 2013-14.

18.1 It is submitted that the revenue treated the consultancy fees paid as "fee for technical services", thereby disallowing the expenditure under section 40(a)(ia) of the Act. The Ld.AR submitted that, none of these non-resident companies have any permanent establishment in India and that, the nature of services rendered does not fall into the category of any managerial, technical or consultancy services (including the provision of services of technical or other personal)

18.2 The Ld.AR placed reliance on various provision in the respective treaties in order to support its contention that, no tax is to be deducted on such payments.

18.3 On the contrary, the Ld.CIT.DR relied on orders passed by authorities below. It is submitted that assessee paid to various consultants in Australia, Brazil, Japan, Singapore and USA towards the services rendered by the parties. The Ld.CIT.DR submitted that, for assessment in 2013-14 the assessee paid recruitment charges amounting to ₹ 1,08,69,631/-, out of which ₹ 38,75,435/- was paid without deducting TDS.

18.4 We have perused submissions advanced by both sides in light of records placed before us.

18.5 We note that, the revenue has not considered the agreements between the assessee and various parties located in different jurisdictions *qua* the DTAA, in order to ascertain the real character

of the payment made. In the interest of justice, we remand these issues for both years under consideration back to the Ld.AO to consider it *de novo* in the light of the agreements entered into by the assessee with various parties having regard to the benefits, available to the assessee under the respective treaties. The assessee is directed to file all requisite details in support of its contention. The Ld.AO shall consider the evidence is filed in accordance with law by granting proper opportunity of being heard to the assessee. The Ld.AO shall take a view considering various decisions passed by this *Tribunal* as well as *Hon'ble Supreme Court* and *High Court*.

Accordingly, Ground No.4 for assessment in 2012-13 and Ground No.3 for assessment year 2013-14 stands allowed for statistical purposes.

19. Disallowance of Software payment: This issue is relevant for assessment year 2013-14 only.

19.1 The assessee claimed depreciation of ₹ 3,61,107 on purchase of computer software amounting to ₹ 10,29,822/-. The Ld.AO disallowed the depreciation under section 40(a)(ia) of the Act, by holding that the computer software was purchased without making TDS on the amount paid to the supplier. The Ld.AO relied on decision of *Hon'ble Mumbai Tribunal* in case of *V Kay Translines (P) Ltd* in *ITA No. 1562/Mum/2010*.

19.2 The Ld. CIT(A) upheld the disallowance by observing as under:

> *"4.8 In view of above, the purchase of software of the appellant is only revenue in nature and the payment for the same cannot be allowed for failure to deduct tax as per the provisions of the Act. The fact that every year the*

appellant is purchasing such software, indicates the revenue nature of such expenditure and adds to the credence of the above conclusion. Therefore, the AO is directed to disallow the payment of Rs 10,59,229 for software u/s 40(a)(ia) of the Act for non compliance of TDS provision. Thus, this will result in enhancement of the disallowance to that extent. Therefore, the ground of appeal by the appellant is dismissed."

19.3 The Ld.AR before this *Tribunal* submitted that, provisions of section 40(a)(ia) of the Act, apply only if the expenditure is claimed as deduction. It is submitted that, in the present facts of the case this condition is not satisfied, since the assessee capitalised the purchase cost of software and depreciation was claimed on the same.

19.4 The Ld.AR submitted that, depreciation is a statutory deduction on the asset which is wholly or partly owned by the assessee and used for the purpose of business. It is submitted that, the deduction under section 32 of the Act is not in respect of the amount paid or payable which is subjected to TDS, but as a statutory deduction on an asset which is otherwise eligible for deduction of depreciation. The Ld.AR emphasised that, depreciation is not an outgoing expenditure, and therefore, the provisions of section 40(a)(i)/(ia) of the Act are not attracted.

19.5 On the contrary, the Ld.CIT.DR relied on orders passed by authorities below.

19.6 We have perused submissions advanced for both sides in light of records placed before us.

19.7 In the facts of the present case, admittedly, the assessee capitalised the cost of the software purchased, on which no tax was deducted at source. It is also an admitted fact that, depreciation is not an outgoing expenditure, and therefore,

provisions of section 40 (a)(i)/(ia) cannot be attracted. We draw support from the decision of *Coordinate Bench* of this *Tribunal* in case of, *Kawasaki Microelectronics vs. DDIT* reported in *(2015) 9 TMI 9.*

19.8 We therefore direct the Ld.AO to delete the addition made in the hands of the assessee.

Accordingly this ground raised by assessee for assessment year 2013-14 stands allowed.

20. <u>Ground No.2: Disallowance of provision for assessment year 2012-13</u>

20.1 The assessee created provision of ₹ 29,39,905/- towards advertisement charges for assessment year 2012-13. The provision created was in respect of services that was received by the assessee, which was reversed on the 1st day of subsequent year. The Ld.AO disallowed the provision by holding that, they were uncrystallised liability. This view was sustained by the Ld. CIT(A).

20.2 Before this *Tribunal,* the Ld.AR submitted that, the assessee regularly follows mercantile system of accounting and business income was computed accordingly. It was submitted that, there is no income attributable to the payee and the provisions are reversed at the very beginning of the next accounting year and therefore the TDS provisions are not applicable. In support, he placed reliance on the decision of *Hon'ble Karnataka High Court* in case of *Karnataka Power Transmission Corporation Ltd* reported in *(2016)67 taxman.com 259* and decision of *Hon'ble Mumbai Tribunal* in case of *Pfizer Ltd in ITA number 1667/Mum/2010.*

20.3 The Ld.CIT.DR relied on orders passed by authorities below.

20.4 We have perused submissions advanced by both sides in light of records placed before us.

20.5 Admittedly, the provisions were made at the end of the year since the invoices were not received up to 31/03/2012. The said provision was reversed in the beginning of the next accounting year. We note that, *Hon'ble Karnataka High Court* in case of *Karnataka Power Transmission Corporation Ltd (supra)* had an occasion to consider identical issue. On perusal of the said decision it is noted that, the assessee therein created provision for contingent payment of interest on belated payments to its suppliers. The assessee therein treated during the years the provision as expenditure, to arrive at profit, but in the return of income filed, the assessee therein did not treat the said amount of provision towards contingent interest payable as expenditure, and arrived at taxable income without excluding such amount of provision. Subsequently, corresponding reversal of entries were made in the books of account during the subsequent financial year. The *Hon'ble Court* directed the disallowance to be deleted.

20.6 Another decision of coordinate bench of this *Tribunal* in case of *M/s.Bosch Ltd vs ITO* in *ITA No.1583/B/2014 dated 01/03/2016*, it is noted that provisions were made at the end of the year and the same was reversed in the beginning of the next accounting year which was allowed.

20.7 In the present facts of the case, we note that, the provision was in respect of a contingent liability for which invoices had not received.

20.8 Under such situation, there is no accrual of income in the hands of the payee and that assessee immediately reverses it on the 1st day of the next accounting year even before the amount accrued to the payee. Therefore, in our view the ratio laid down by *Hon'ble Karnataka High Court* in case of *Karnataka Power Transmission Corporation (supra)*, squarely applies to the present facts of the case.

20.9 Respectfully following the same, way direct the Ld.AO to delete the disallowance made in respect of the provision, that was made on the last day of the financial year relevant to assessment year under consideration, that stood reversed on the 1st day of next accounting year.

Accordingly, Ground no.2 raised by assessee for assessment in 2012-13 stands allowed.

21. <u>Ground No. 3: Disallowance of subsidiary for assessment year 2012-13.</u>

21.1 The assessee incurred ₹ 1,59,450/- towards professional fees for establishing a subsidiary in Australia the Ld.AO disallowed the some treating it to be capital in nature, which was upheld by the Ld.CIT(A) by observing as under:

> *"7.2 During the appellate proceeding, the authorised representative was confronted with the fact that disallowance of subsidiary establishment expenses treating it as capital expenditure, is an admitted fact which has been agreed upon by the appellant during the assessment proceeding and thus the same should not he made a subject matter of appeal. The authorised representative also appreciated the factual position and acknowledged that the same was admitted at assessment stage In view of this, the ground number 3 of the appeal is not adjudicated and is treated as dismissed."*

21.2 Before this *Tribunal* the Ld.AR relied on decision of coordinate bench of this *Tribunal* in case of *On Mobile Global Ltd vs DCIT* in *ITA number 1163/B/2012*.

21.3 We have perused the said decision relied by the Ld.AR. We note that, in that case *Tribunal* was considering an issue where assessee therein had made payment towards the due diligence and feasibility study conducted by a consultant before acquiring a company. Whereas, in the present facts of the case the expenditure has been incurred by assessee in order to establish a subsidiary company in Australia. This is an expenditure incurred for expanding assessee's business and has been rightly treated as capital in nature by the revenue authorities. We therefore do not find any infirmity in the view taken by the Ld.CIT(A).

Accordingly this ground raised by assessee for assessment in 2012-13 stands dismissed.

In the result appeal filed by assessee for assessment year 2012-13 stands partly allowed for statistical purposes and appeal filed for assessment year 2013-14 stands allowed for statistical purposes.

Order pronounced in the open court on 29th April, 2022.

Sd/-	Sd/-
(CHANDRA POOJARI)	(BEENA PILLAI)
Accountant Member	Judicial Member

Bangalore,
Dated, the 29th April, 2022.
/MS /

Copy to:

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR, ITAT, Bangalore
6. Guard file

By order

Assistant Registrar,
ITAT, Bangalore