

आयकर अपीलीय अधिकरण, हैदराबाद पीठ में
IN THE INCOME TAX APPELLATE TRIBUNAL
HYDERABAD BENCHES "B", HYDERABAD

BEFORE
SHRI RAMA KANTA PANDA, ACCOUNTANT MEMBER
&
SHRI K.NARASIMHA CHARY, JUDICIAL MEMBER

आ.अपी.सं / ITA No. 1410/Hyd/2019
(निर्धारण वर्ष / Assessment Year: 2016-17)

Dy. Commissioner of
Income Tax,
Circle-16(1),
Hyderabad

M/s. Nipro Medical India
Vs. Private Limited,
Hyderabad
[PAN No. AACCN4008J]

अपीलार्थी / Appellant

प्रत्यर्थी / Respondent

निर्धारित द्वारा/Assessee by: Shri Kishor Phadke, AR
राजस्व द्वारा/Revenue by: Shri Naveen Kumar, DR

सुनवाई की तारीख/Date of hearing: 03/11/2022
घोषणा की तारीख/Pronouncement on: 15/12/2022

आदेश / ORDER

PER K. NARASIMHA CHARY, JM:

Challenging the order dated 27/06/2019 passed by the learned Commissioner of Income Tax (Appeals)-4, Hyderabad ("Ld. CIT(A)") in the case of M/s. Nipro Medical India Private Limited ("the assessee") for the assessment year 2016-17, Revenue preferred this appeal.

2. Brief facts of the case are that the assessee is engaged in the business of trading of various medical equipments and consumables. They have filed their return of income on 30/11/2016 admitting loss of Rs.

7,36,04,831/- and a loss at Rs. (-)23,87,15,864/- under section 115JB of the Income Tax Act, 1961 (for short "the Act"). Assessment under section 143(3) of the Act was complete by order dated 22/12/2018 determining the loss at Rs. 4,33,40,323/- by making addition of Rs. 3 crores which the assessee paid to one M/s Atlantic Pharmaceuticals towards contractual breach, by holding that it was in the nature of penalty and Rs. 2,64,508/- towards the delay deposit of the provident fund collected from the employees, beyond the stipulated date to the Government account.

3. Aggrieved by such an action of the learned Assessing Officer, assessee preferred an appeal before the Ld. CIT(A) and contended that the payment of Rs. 3 crores made by the assessee was not in the nature of penalty or fine but it was the amount that was paid pursuant to the mutual agreement of the parties to terminate the civil suit and in accordance with the order of the Arbitrator, it is in the best interest of business of the assessee and, therefore, allowable under section 37(1) of the Act. In respect of the provident fund amount deposited with the delay, assessee contended that since it was deposited before the due date for filing of the return, the same was allowable.

4. Having considered the contentions of the assessee in the light of the facts narrated, Ld. CIT(A) was of the opinion that the payment of Rs. 3 crores was to be allowed as business expenditure, inasmuch as it was paid to make the contractual obligation and that too through proper arbitration and, therefore, in the light of the decision reported in Birla Cotton Spinning and Weaving Mills Ltd vs. CIT (1967) 64 ITR 568 (Cal) and CIT vs. Navsari Cotton and Silk Mills Ltd (1982) 135 ITR 546 (Guj), the same is allowable as an expenditure. Ld. CIT(A) deleted the addition made on account of the late payment of PF also.

5. Challenging the order of the Ld. CIT(A) in respect of the addition of Rs. 3 crores under section 37(1) of the Act, Revenue is in this appeal. It is contended by Ld. DR that there was no trading activity of the assessee

during the period of assessment year 2015-16 and years prior to the assessment year 2015-16 inasmuch as the assessee started trading business only from financial year 2015-16 relevant to the assessment year 2016-17; that even the contract said to have been breached was not between the assessee and M/s Atlantic Pharmaceuticals but it was between M/s Nipro India Corporation Pvt. Ltd and M/s Atlantic Pharmaceuticals; and that therefore, the said amount paid by the assessee cannot be said to be for the purpose of business of the assessee.

6. Per contra, it is the submission of the Ld. AR that the assessee was formed as 100% subsidiary of the Nipro Corporation in the financial year 2006-07 itself for the purpose of marketing and supply of Nipro products in India but it is only till the manufacturing activity of Nipro group started in India, the trading activity the assessee was looked after by M/s Nipro India Corporation Pvt. Ltd, and when once the manufacturing activity had started, all the trading assets and trading liabilities, including third party claims relating thereto, were transferred to the assessee, and therefore, the assessee is justified in making the payment pursuant to the arbitration award.

7. We have gone through the record in the light of the submissions made on either side. Nipro Corporation (Japan) was selling bulk needles, pack needles etc. in India through a third party distributors by name M/s Atlantic Pharmaceuticals till 2005-06. In the financial year 2006-07, they formed the assessee for the purpose of marketing and supply of Nipro products in India. In the financial year 2010-11 M/s Nipro India Corporation Pvt. Ltd. was formed for the purpose of manufacturing activity. It was, however, thought by the Nipro Corporation (Japan) that till the manufacturing activity takes place in India, the Nipro India Corporation Pvt. Ltd shall carry on the trading activity of the Nipro products and later on the said task was to be undertaken by the assessee. In view of the trading activity undertaken by the Nipro Corporation through one of its subsidiary, the business of M/s Atlantic Pharmaceuticals was reduced and,

therefore, M/s Atlantic Pharmaceuticals brought a suit before the Madras High Court against the Nipro India Corporation Pvt. Ltd. Having realised the futility of litigation, both the parties opted to approach an Arbitrator and accordingly the matter was referred to arbitration. In the meanwhile, assessee undertook the activity of trading activity. In the circumstances, when the order of the Arbitrator was passed for a sum of Rs. 3 crores payable by Nipro Corporation to M/s Atlantic Pharmaceuticals, the assessee paid the said amount, and claimed the same as business expenditure.

8. Insofar as the facts are concerned, absolutely there is no dispute. Though it is contended on behalf of the Revenue that the assessee was not conducting the trading activity in the financial year 2015-16, is not in dispute that such trading activity was conducted on behalf of the assessee by M/s Nipro India Corporation Pvt. Ltd. It is not in dispute that the order of the Arbitrator was passed on 9/12/2015 by which date the assessee commenced the trading activities. It is the submission on behalf of the assessee that it was in the business interest of the assessee that the amount under the arbitration award was paid by the assessee which is the obligation of the Nipro Corporation.

9. According to the learned Assessing Officer such an expenditure is in the nature of penalty or fine and, therefore, not allowable as business expenditure under section 37 (1) of the Act. Explanation 1 to section 37 (1) of the Act reads that any expenditure incurred by an assessee for any purpose which is an offence or which is prohibited by law shall not be deemed to have been incurred for the purpose of business or profession and no deduction or relevance shall be made in respect of such expenditure. Insofar as the facts of this case are concerned, by no stretch of imagination could it be said that the amount paid pursuant to the arbitration award on the allegation of M/s Atlantic Pharmaceuticals that there was breach of obligation pursuant to a contract, can be said to be for the purpose of any offence or that the same is prohibited by any law.

Breach of contractual obligation cannot be said to be an offence under any law.

10. Ld. CIT(A) referred to the terms of the consent signed by the parties submitted before the Arbitrator and found that it was for payment of settled compensation by the assessee to save future litigation costs and to save brand image in the market, apart from the fact that the distribution agreement reads that in the event of dishonesty, poor performance and/or violation of any provision of the agreement by either party, both the parties shall do their best effort to settle the matter in dispute in a prompt and amicable manner, and that there is no mention of any penal clause/action in the event of violation of any provisions of the agreement. Basing on this, Ld. CIT(A) concluded that the payment was towards discharge of the liability as contractual obligation and the transaction does not constitute any offence, nor is it prohibited by law.

11. Insofar as the argument that the assessee was not a party to the agreement said to have been breached, it could be seen from the record that the primary objective of the assessee is to carry on the trading activities of M/s Nipro Corporation in India, and it is only till the commencement of the manufacturing activity, the avowed objective of the assessee was looked after by M/s Nipro India Pvt. Ltd. As a matter of fact, Nipro India Pvt. Ltd was also constituted in the financial year 2010-11 whereas the assessee was formed in the financial year 2006-07 itself. In the financial year 2005-06, M/s Atlantic Pharmaceuticals was looking after the development of Indian market for Nipro products. It is, therefore, clear that, when the trading activity of Nipro Corporation (Japan) was carried out in India by M/s Atlantic Pharmaceuticals, and subsequently for the very same purpose the assessee was formed in the financial year 2006-07, on the transfer of the trading assets and trading liabilities, including 3rd party claims relating thereto, the assessee acquired the entire package which shall include the obligation to pay the amounts under the arbitration award.

12. It could be seen from the record that the Ld. CIT(A) referred to the decision of the Hon'ble Apex Court in the case of Navsari Cotton (supra) wherein the Hon'ble High Court evolved the tests on principles to claim deduction of an expenditure as business expenditure, and it includes, the expenditure incurred with a view to bring profits or monetary advantages today or tomorrow, to render the assessee immune from impending or reasonably apprehended litigation, in order to save losses in foreseeable future, for affecting economy in working which may pay dividends today or tomorrow, for increasing efficiency and working and for removing inefficiency in the working.

13. When viewed from the angle of the tests formulated by the Hon'ble Gujarat High Court in Navsari Cotton (supra) it is clear that the amounts paid by the assessee to M/s Atlantic Pharmaceuticals fall in the category of the expenditure incurred by the assessee to make it immune from the impending or reasonably apprehended litigation, and to save losses in foreseeable future in the shape of damage to the brand image in the market. With this view of the matter, we are of the considered opinion that the Ld. CIT(A) is right in his approach. As stated supra, by no stretch of imagination could it be said that the payment for breach of contractual obligation pursuant to an arbitration award in the pending litigation, cannot be said to have been incurred for any purpose which is an offence or which is prohibited by law. With this view of the matter, we uphold the findings of the Ld. CIT(A) and decline to interfere with the same.

14. In the result, appeal of the Revenue is dismissed.

Order pronounced in the open court on this the 15th day of December, 2022.

Sd/-

(RAMA KANTA PANDA)
ACCOUNTANT MEMBER

Hyderabad, Dated: 15/12/2022

Sd/-

(K. NARASIMHA CHARY)
JUDICIAL MEMBER

TNMM

Copy forwarded to:

1. The Dy.Commissioner of Income Tax, Circle-16(1), Hyderabad.
2. M/s. Nipro Medical India Private Limited, 2nd Floor, GMR Aero Towers, Rajiv Gandhi International Airport, Shamshabad, Hyderabad.
3. CIT(A)-4, Hyderabad.
4. Pr.CIT-4, Hyderabad.
5. DR, ITAT, Hyderabad.
6. GUARD FILE

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ASSISTANT REGISTRAR
ITAT, HYDERABAD