INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH "A": NEW DELHI
BEFORE Shri C.M. Garg, Judicial Member
AND
Dr. B. R. R. Kumar, Accountant Member

ITA No. 6707/Del/2018
(Assessment Year: 2012-13)

Addl. CIT, Special Range-1, New Delhi (Appellant)	Vs.	Amway India Enterprises Pvt. Ltd, 1st Floor, Plot NO. 8, Elegance Tower, Jasola, New Delhi -110025 (Respondent)

PAN: AAACA5603Q

Assessee by :	Sh. Sudesh Garg, Adv Sh. Prince Bansal, CA Ms. Bhavya Garg, CA
Revenue by:	Sh. P. Praveen Sidharth, CIT DR
Date of Hearing	16/02/2023
Date of pronouncement	08/05/2023

O R D E R

PER C. M. GARG, J. M.:

1. This is an appeal filed by the revenue against the order of the ld CIT(A)-11, New Delhi dated 27.04.2016 for AY 2012-13.

2. The effective ground No. 1 and 2 of the revenue reads as under:-

"i) The Ld CIT(A) erred in law and on facts in deleting the addition of Rs. 38,12,22,446/- on the account of amounts written off and treating the expenditure as revenue expenditure.

ii) The Ld. CIT(A) erred in deleting the abovementioned addition despite the fact that the assessee could not prove business expediency of the expenditure under reference."

3. The ld CIT DR supported the assessment order and submitted that a plain reading of section 37(1) of the Act shows that to be an allowable expenditure under this provision, the amount of expenditure incurred by the assessee must be (a) paid out of wholly and exclusively for the purpose of business or profession of assessee, (b) must not be capital expenditure, or

personal expenses or an allowance of the character described in section 32 to 36 of the Act.

4. The ld DR submitted that in the present case distributors of the assessee were receiving commission income for their services and were liable to pay service tax on such services as per relevant rules. The ld DR submitted that, in addition to commission, the assessee provided financial assistance to ABOs in the form of loan for discharging service tax liability and the amount debited to the account of ABO and subsequently the assessee written off these loans and the assessee claimed the same as revenue expenditure being bad debts. The ld DR submitted that the net effect of the said accounting of claim of assessee was effectively that the assessee assumed liability of services tax which was not payable to him but was payable to the ABOs/ distributors. The ld DR submitted as per judgment of the Hon'ble Supreme Court in the case State of Madras Vs. G.J. Coelho (1964) 53 ITR 186, wherein, it was held that the expenditure made under a transaction which is so closely related to the business that it could be viewed as on integral part of the conduct of business, may be recorded as revenue expenditure laid out wholly and exclusively for the purpose of business. The ld DR submitted that the AO was right in disallowing the payment of service tax by the assessee to its distributors showing the same as debts and subsequently treating the same as bad debts is a clear example of claiming revenue expenditure in the garb of bad debts which is not permissible in the law. The ld DR lastly submitted that the AO has rightly disallowed the impugned amount and added back to the total income of the assessee being not wholly and exclusively incurred for the purpose of business of the assessee. Therefore, the AO was right in making addition in the case of the assessee. The ld DR prayed that the ld CIT(A) has granted the relief to the assessee without any basis therefore, the impugned first appellate order may kindly be set aside by restoring that of the AO.

5. Replying to the above, ld counsel of the assessee submitted that the assessee is a company is working through its distributors and the chain of distributors is sole source of the assessee to reach its customers. The ld

counsel submitted that there was service tax liability created on the distributors due to application of new GST Rules and distributors were facing great hardship in making payment of service tax out of the commission income earned by them. The ld counsel submitted that keeping in view the hardship of the distributors the assessee company decided to support their distributors by way of payment of services tax and the amount paid to them was shown as debit balance in their respective account with an expectation that within same time this amount would be settled. The ld counsel submitted that specifically it was observed by the assessee company that the distributors/ ABOs are not able to return the amount debited to their respective accounts, therefore, the same was treated as bad debts and claim granted in the profit and loss account of the assessee. Ld counsel submitted that in the present case the appellant has made the payment of service tax to the ABOs for smooth running of business by facilitating its distributors to pay the service tax liability and since the legality of said liability was not clear, the payment was shown as loan in the books of account if assessee and not claimed as an expenditure on account of service tax in the year of payment. The ld counsel submitted that the Hon'ble Supreme Court in the case of State of Madras Vs. GJ Coelho (supra) as noted by the AO in para 3 and 4 of the assessment order, it was held that the expenditure made under the transaction which is so closely related to the business of the assessee that it can be viewed as integral part of conduct of the business, may be regarded as revenue expenditure laid out wholly and exclusively for the purpose of the business.

6. The ld counsel submitted that there is no denial of the fact that the payment was made to the distributors for reimbursement of service tax liability borne by them and it has been exclusively demonstrated by the assessee that the payment was made only to those ABOs who had actually paid the service tax. Ld counsel submitted that in view of the foregoing factual position and compulsion of the assessee the appellant has made payment to its distributors to sustain their survival and existence the amount paid by the appellant, which was subsequently written off as bad

debits is closely related to the business activity of the assessee and thus it was incurred wholly and exclusively for the purpose of the business of the assessee and the same was not capital or personal expenditure, therefore, the ld CIT(A) was right in allowing the claim of the assessee considering the entire facts and circumstances and commercial expediency of business of the assessee. The ld counsel lastly submitted that the findings arrived by the ld CIT(A) are quite correct and sustainable therefore, impugned first appellate order may kindly be upheld dismissing the ground of revenue.

7. On careful consideration of the above submission, first of all we find it necessary and appropriate to reproduce the relevant operative part of the first appellate order which reads as under:-

> *"5.3 I have gone through the facts of the case and the submission made by the AR. It has been contended that the appellant is selling the goods directly to customers through independent distributors who are known as Amway Business Owners (ABOs). The ABOs are entitled to commission as per their entitlement. Earlier no Service Tax was being charged and paid by the ABOs but later on, the ABOS started receiving quarries from the Service Tax Department on the ground that they are taxable under the category of Business Auxiliary Services. However, the issue of liability of the Service Tax was not clear. Since the Service Tax Department was asking the ABOS to pay the Service Tax, the ABOS asked the appellant company for help as the ultimate liability of Service Tax is to be borne by the person who avails the services. It is further submitted that the appellant, in view of the above facts, decided to lend certain amount to the ABOS for the amount to be paid as Service Tax by them till the issue of taxation with the Department get settled. The said amount was not claimed in the P&L account as an expense at that time as the issue of applicability of Service Tax was not final and therefore, the appellant company had shown these amounts as loans to the ABOS in its balance sheet. The AR has submitted that the CBEC finally clarified on 03.06.2009 that the services provided by the ABOS was taxable. In view of this, the ABOS requested the appellant to waive off the refundable loan because they had already paid the said amount to the Service Tax Department. After considering all the factors, the appellant decided to write off the amounts paid to the ABOS for meeting the Service Tax liability ull December 2011. As already discussed, the AO has disallowed this amount written off and has made the addition by holding that this sum was not wholly & exclusively incurred for the purposes of the business and also the same is in the nature of capital expenditure.*
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> *5.3.1 From the above facts, in order to decide the allowability of the amount written off by the appellant during the year under consideration, the following issues need to be deliberated:*
>
> *Whether the expense claimed by the appellant is capital in nature; Whether the appellant was right in claiming the amount in this year;*

Whether there was any business/commercial expediency and whether the expense was incurred wholly and exclusively for the purposes of its business.

Each of these aspects is discussed as under.

5.3.2 Capital or Revenue:

It is observed that the appellant company had made available the funds to the ABO's for making payment of the service tax liability and it was shown in the accounts under the head of loans and advances because it was not clear whether the service tax is liable to be paid by the ABOS or not. The appellant was asked whether the said payment was made to all the ABOS in response to which the AR has submitted the complete list of the ABOS to whom this advance payment was paid and which has been written off. It has been submitted that the advances given are not round figures but have been worked out after verification of service tax burden of the relevant ABO. Advances have been extended to around five hundred such ABOs. At the time of write off, further verification was made by the appellant and only in those cases where service tax was found to have been paid, were written off. It is to be observed that in order to treat an expenditure as capital in nature, it should result in some enduring benefits to the appellant or creation of some asset. Reference is made to the decision of Hon'ble Supreme Court in the case of Empire Jute Co Ltd vs CIT (1980)124 ITR 1, In which it has been held that-

There may be cases where expenditure, even if incurred for obtaining advantage of enduring benefit, may, none the less, be on revenue account and the test of enduring benefit may break down. It is not every advantage of enduring nature acquired by an assessee that brings the case within the principle laid down in this test. What is material to consider is the nature of the advantage in a commercial sense and it is only where the advantage is in the capital field that the expenditure would be disallowable on an application of this test. If the advantage consists merely in facilitating the assessee's trading operations or enabling the management and conduct of the assessee's business to be cared on more efficiently or more profitably while leaving the fixed capital untouched, the expenditure would be on revenue account, even though the advantage may endure for an indefinite future. The test of enduring benefit is, therefore, not a certain or conclusive test and it cannot be applied blindly and mechanically without regard to the particular facts and circumstances of a given case. But even if this test were applied in the present case, it does not yield a conclusion in favour of the revenue. Here, by purchase of loom hours no new asset has been created. There is no addition to or expansion of the profit-making apparatus of the assessee. The income earning machine remains what it was prior to the purchase of loom hours. The assessee is merely enabled to operate the profit making structure for a longer number of hours. And this advantage is clearly not of an enduring nature. It is limited in its duration to six months and, moreover, the additional working hours per week transferred to the assessee have to be utilised during the week and cannot be carried forward to the next week. It is, therefore, not possible to say that any advantage of enduring benefit in

the capital field was acquired by the assessee in purchasing loom hours and the test of enduring benefit cannot help the revenue

When dealing with cases of this kind where the question is whether expenditure incurred by an assessee is capital or revenue expenditure, it is necessary to bear in mind what Dixon, J. said in Hallstrom's Property Limited v. Federal Commissioner of Taxation(1): "What is an outgoing of capital and what is an outgoing on account of revenue depends on what the expenditure is calculated to effect from a practical and business point of view rather than upon the justice classification of the legal rights, if any, secured, employed or exhausted in the process....

The question must be viewed in the larger context of business necessity or expediency. If the outgoing expenditure. is so related to the carrying on or the conduct of the business that it may be regarded as an integral part of the profit- earning process and not for acquisition of an asset or a right of a permanent character, the possession of which is a condition of the carrying on of the business, the expenditure may be regarded as revenue expenditure. See Bombay Steam Navigation Co. (1953) Pvt. Ltd. v. Commissioner of Income-tax(2) The same test was formulated' by Lord Clyde in Robert Addze & Son's Collieries Ltd. v. Inland Revenue(3) in these words: Is it part of the company's working expenses, is it expenditure laid out as part of the process of profit earning ? or, on the other hand, is it a capital outlay, is it expenditure necessary for the acquisition of property or of rights of permanent character, the possession of which is a condition of carrying on its trade at all ?" It is clear from the above discussion that the payment made by the assessee for purchase of loom hours was expenditure laid out as part of the process of profit- earning. It was, to use Lord Soumnar's words, an outlay of a business in order to carry it on and to earn a profit out of this expense as an expense of carrying it on. It was part of the cost of operating the profit earning apparatus and was clearly in the nature of revenue expenditure."

Similarly, the Apex Court had an occasion to consider an identical issue in the case of CIT vs. Kalyanji Mavji & Co. (1980) 122 ITR 49. In the case before the Apex Court, the assessee incurred the expenditure on payment of surface rent, minimum royalty and on account of salary for the watch and ward and claimed it as a business expenditure. The assessee has also incurred expenditure for renovating the building, reconditioning of machinery and clearing of debris. The assessee claimed the expenditure as revenue expenditure. The Apex Court after referring to earlier decision in the case of Assam Bengal Cement Co. Ltd. vs. CIT(1955) 27 ITR 34 found that the expenditure incurred by the assessee was in the process of profit earning. Therefore, it was allowed as revenue expenditure.

In the present case, the appellant has not acquired any capital asset and has not got any benefit of enduring nature by making this payment but the payment was made for smooth running of the business by facilitating its distributors to meet the Service Tax liability. Just because the amount was shown as loan in the balance sheet does not give it a character of "capital in nature". In view of these facts, I am of the view that the amount paid by the appellant and subsequently written off is closely related to the business

activities and therefore, the same needs to be treated as revenue expenditure.

5.3.3 Year of Claim

From the details furnished by the AR about the payment made to the distributors, it is observed that the payment was made during the FYS 2007-08 to 2011-12. The appellant had created a provision of Rs. 28,05,40,581/- during the FY 2010-11 and the balance of Rs. 10,06,81,865/- in FY 2011-12 and the total amount of Rs. 38,12,22,446/- has been claimed in the year under consideration. With respect to the issue of the year in which the claim can be allowed, the AR has submitted that the liability of the service tax for the nature of business of the appellant was disputed and many distributors were being forced to pay the service tax and the same was being done by some distributors and since the ultimate liability of payment of service tax lied upon the appellant, the appellant had made the payment to these distributors who were made to deposit service tax. In the accounts, the appellant company recorded these payments as loan, although it was not actually a loan. It is further contended that the appellant wanted the distributors to contest the service tax liability with the department and therefore, it had stated the payment to be in the nature of refundable loan. In the year under consideration, the appellant reconciled to the fact that service tax liability was mandatory and cannot be avoided and therefore, it decided to waive of the amount of refundable advances paid to the distributors earlier. In addition, the AR has furnished the details of the total income and tax paid by the appellant during the last five years from which it is observed that the appellant has shown positive profit in all these years and has been paying the tax at the maximum marginal rate. By doing so, the AR has contended that the claim is revenue neutral with respect to the year of claim. Based on these facts, I am of the view that the claim made by the appellant during the year consideration is justified.

5.3.4 Business expediency/expenditure incurred for the purposes of the business

In this regard, it has been submitted that that ABOS are very essential to the successful running of the business of the appellant. The appellant company has made available the funds to the ABOS for making payment of the service tax liability because they had no such capability to make the payment of service tax liability. If the funds would not have been made available by the appellant, they would have been forced to stop working for the company and the business of the company would have severely suffered. The AR has stated that there cannot be any better evidence of the business expediency than the fact that the business of the appellant would have collapsed if the funds for payment of service tax were not made available by the appellant. In this regard, it has to be appreciated that the financial burden of the service tax is always on the person who avails of the services. In the instant case there is no dispute that the services have been availed by the appellant and the appellant was liable to reimburse that to the service providers i.e. the ABOS.

Reference is made to the decision of Hon'ble Apex Court in CIT Vs. Bharat Carbon & Ribbon Mfg. Co. (P) Ltd., 1999 XII SITC 218 wherein it has been observed that whether the assessee is entitled to a particular deduction or not will depend on the provision of law relating thereto and not on the view which the assessee might take of his rights nor can the existence or absence of entries in the books of accounts be decisive or conclusive in the matter. The expression "wholly" in section 37(1) has been used with reference to the quantum, while the expression 'exclusively' refers to the nature or the purpose of the activity in which the expenditure is incurred. In other words, the whole of the expenditure must have been solely and exclusively incurred for business purposes, in order to qualify for allowance under section 37(1) of the Act. The expression "Wholly & exclusively used in section 10(2) (xv) of the Income-tax Act, 1922 (Which corresponds to section 37(1) of the Income-tax Act, 1961) does not mean "necessary". Ordinarily, it is for the assessee to decide whether any expenditure should be incurred in the course of his or its business. Such expenditure may be incurred voluntarily and without any necessity and if it is incurred for promoting the business and to earn profits. The assessee can claim deduction even though there was no compelling necessity to incur such expenditure. (Sasson J. David & Co. (P) Ltd. Vs. CIT (1979) 118 ITR 261 (SC)). Thought the main objects of business are to earn profits, business purposes are wider than profit-making purposes. Business expediency does not require that expenses should be incurred only for earning immediate profits. Expenses incurred though not directly related to earning to income, may be allowable deductions if they are related to the carrying on of the business (Birla Cotton Spinning & Weaving Mills Ltd. Vs. CIT (1967) 64 ITR 568 (Cal)). It is for the assessee to decide how best to protect his own interest. It is not open to Income-tax department to prescribe what expenditure an assessee should incur and in what circumstances he should incur that expenditure (CIT Vs. Dhanrajgiri Raja Narasingiri (1973) 91 ITR 544 (SC)). Expression "commercial expediency is not a term of art. It means everything that serves to promote commerce and includes every means suitable to that end. Commercial men are best experienced in commercial expediency (Indian Steel & Wire Products Ltd. Vs. CIT (1968) 69 ITR 379 (Cal)). In applying the test of commercial expediency for determining whether the expenditure was wholly and exclusively laid out for the purposes of the business, reasonableness of the expenditure has to be adjudged from the point of view of the businessman and not of the revenue (Jamshedpur Motor Accessories Stores Vs. CIT (1974) 95 ITR 664 (Pat); J.K. Woollen Manufacturers Vs CIT (1969) 72 ITR 612 (SC). In order that an expenditure may be admissible as a deduction under section 10(2)(xv), it is not necessary that the primary motive in incurring it must be directly to earn income thereby (Sree Meenakshi Mills Ltd. Vs. CIT (1967) 63 ITR 207 (SC). In CIT Vs. Malayalam Plantations Ltd. (1960) 53 ITR 140, the Supreme Court has observed at page 150, that:

"The expression for the purpose of the businesses is wider in scope than the expression 'for the purpose of earning profits. Its range is wide, it may take in not only the day to day running of a business but also the rationalisation of its administration and modernisation of its machinery, it may include measures for the preservation of the business and for the protection of its assets and property from expropriation, coercive process or assertion of hostile; it may also comprehend payment of statutory dues and taxes

imposed as a precondition to commence or for the carrying on of a business; it may comprehend many other acts incidental to the carrying on of a business. However wide the meaning of the expression may be, its limits are implicit in it. The purpose shall be for the purpose of the business, that is to say, that expenditure incurred shall be for the carrying on of the business and the assessee shall incur it in his capacity as a person carrying on the business. It cannot include sum spent by the assessee as agent of a third party, whether the origin of the agency is voluntary or statutory"

In the present case, the appellant has made the payment for smooth running of the business by facilitating its distributors to meet the Service Tax liability and since the legality of the said liability was disputed, the payment was shown as a loan in the books of account and not claimed as an expenditure on account of Service Tax in the year of payment. However, there is no denial of the fact that the payment was made to the distributors for reimbursement of the Service tax liability borne by them. It has been shown by the appellant that the payment was made only to those ABOS who had actually paid the Service Tax, although it was paid under protest. In view of these facts, I am of the view that the amount paid by the appellant and subsequently written off is closely related to the business activities and therefore, the same was incurred due to commercial expediency.

5.3.5 After considering all the above facts and the legal discussion, I am of the opinion that the payments made by the appellant are directly related to the business activities and the claim made by it is allowable as a business expenditure. Accordingly, the addition made by the AO is deleted and ground of appeal is allowed."

8. In view of the above, first of all, we note that there is no quarrel or dispute regarding quantum of expenditure/ bad debts claimed by the assessee. We further noted neither the AO nor the ld CIT DR before us disputed the fact that the assessee made payment of service tax to its distributors who had actually paid the amount of service tax to the exchequer and thus, it was a kind of reimbursement of service tax liability of the assessee to its distributors. It is a fact of common knowledge that the liability of service tax was arose due to application of new taxation of law such as GST and the issue as to whether such liability was to be borne by the distributors of the assessee company or the assessee was not settled up to that point of time. We are in agreement with the contention of the ld counsel of the assessee, as noted that the ld CIT(A) observed that the payment was shown as loan in the books of account and not claimed as an expenditure on account of service tax in the year of payment since the legality of said liability was not clear and disputed. As to whether the liability

has to be borne by the assessee i.e. service receiver or the distributor i.e. service providers. In such a situation when the assessee company has paid amount to its distributors who had actually paid the service tax amount to the exchequer is a kind of adhoc reimbursement of expenditure or liability of service tax. In view of the above factual position without keeping in view the hardship of the distributors and the liability of the services tax the company decided to write off the amount of loan debited to the respective account of the distributors/ ABOs then the ld CIT(A) was right in concluding that the payment was made by the appellant are directly related to the business activity of the assessee and it was incurred wholly and exclusively for the purpose of business of the assessee due to commercial expediency and the same was allowable as business expenditure. We are unable to find any valid reason to interfere with the finding arrived by the ld CIT(A) and thus we uphold the same. Accordingly, effective ground No. 1 and 2 of revenue being devoid of any merit and are dismissed.

9. In the result, the appeal of the revenue is dismissed.

Order pronounced in the open court on 08/05/2023.

-Sd/-	-Sd/-
(B. R. R. Kumar)	**(C. M. GARG)**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

Dated: 08/05/2023
A K Keot

Copy forwarded to

1. Applicant
2. Respondent
3. CIT
4. CIT (A)
5. DR:ITAT

ASSISTANT REGISTRAR
ITAT, New Delhi