आयकर अपीलीय अधिकरण,' बी' न्यायपीठ, चेन्नई

IN THE INCOME TAX APPELLATE TRIBUNAL
'B' BENCH, CHENNAI

श्री चंद्र पूजारी,लेखा सदस्य एवं श्रीजी. पवन कुमार,न्यायिकसदस्यकेसमक्ष

BEFORE SHRI CHANDRA POOJARI, ACCOUNTANT MEMBER AND SHRI G. PAVAN KUMAR, JUDICIAL MEMBER

आयकर अपील सं./I.T.A. Nos.2059 & 2062/Mds/2015

निर्धारण वर्ष /Assessment years :2008-2009 & 2009-2010

The Deputy Commissioner of Income Tax, Corporate Circle 1(1) Chennai 600 034.	**Vs.**	M/s. DSM Soft Private Limited, No.1, 15th Cross Street, Shastri Nagar, Adayar, Chennai 600 020
		[PAN AAACD 3149A]
(अपीलार्थी/Appellant)		**(प्रत्यर्थी/Respondent)**

अपीलार्थी की ओर से/ Appellant by	**:**	Shri. A.B. Koli, IRS, JCIT.
प्रत्यर्थी की ओर से /Respondent by	**:**	Ms. Hemalatha, K. ACA.
सुनवाई की तारीख/Date of Hearing	**:**	13-01-2016
घोषणा की तारीख /Date of Pronouncement	**:**	30-03-2016

आदेश / O R D E R

PER G. PAVAN KUMAR, JUDICIAL MEMBER:

The appeals filed by the Revenue are directed against different orders of Commissioner of Income Tax (Appeals)-1, Chennai dated 27.07.2015 for the above assessment years passed u/s.143(3) r.w.s. 147 and 250 of the Income Tax Act, 1961 (herein after referred to as ''the Act''). Since the issue in these appeals are common in nature,

these appeals are clubbed, heard together, and disposed of by this common order for the sake of convenience.

2. The Revenue has raised the following grounds:-

> *''2.1 The learned CIT(A) erred in deleting the disallowance of interest on borrowed capital diverted for giving interest free loans to the group concerns of the assessee and for investment in the equity shares of the assessee's subsidiary company applying the decision of the Supreme Court in 288 ITR 1 without considering the difference in the facts containing in the assessee's case.*
>
> *3.1 The learned CIT(A) erred in not appreciating the legal fiction created by the clarificatory explanation inserted by the Finance Act, 2012 giving the same retrospective effect from 01.06.1976. The learned CIT(A) ought to have appreciated the intent of the legislature.*
>
> *4.1 The learned Commissioner of Income Tax (Appeals) erred in holding that the business losses of a unit which is not eligible for deduction u/s.10A of the Act could not be set off against the profits of the undertaking eligible for deduction u/s.10A for the purpose of determining the allowable deduction u/s.10A of the act''.*

Since the issues in these two appeals are common in nature, We take up ITA No. 2059/Mds/2015 of assessment year 2008-2009 for adjudication.

3. The brief facts of the case are the assessee is in the business of software development and export and filed return of income for the assessment year 2008-2009 on 30.09.2008 declaring loss of ₹57,15,918/- and was processed u/s.143(1) of the Act. Subsequently notice u/s.148 was issued for reason to believe that income has escaped assessment. In compliance to notice, the ld. Authorised Representative of the assessee appeared on various dates and filed details. The Assessing Officer on perusal of the financial statements of the company found that assessee borrowed secured loans from banks and unsecured loans from Directors and others paid varying interest rates. As per Balance sheet the assessee is having secured loans of ₹15,73,90,542/- and unsecured loans and assessee also paying interest on above loans as per page 2 of Assessing Officer order as under:-

On Bank loans	*1,46,15,759/-*
On other loans	*27,88,064/-*

As per the information, the assessee has given interest free loans to subsidiaries and also invested in group concerns as under:-

> *"DSM Geodata Ltd. ₹5,55,69,765/- (loan/advance)*
> *DSM Infosystems P. Lt ₹2,21,72,376/- (loan/advance)*
> *DCS BPO Pvt. Ltd ₹1,79,45,150/- (loan/advance)*
> *DCS BPO Pvt. Ltd ₹49,58,877/- (investment)"*

The ld. Authorised Representative explained that the assessee company made investment in subsidiary company DSM Geodata Ltd –

Scotland ₹2,52,85,072/-. On perusal of the transaction with related parties, the assessee has not received any interest from associate companies. On further verification it was found that interest of ₹22,70,805/- was received from subsidiary company from DCS Geodata Ltd which has worked out to ₹4.26% interest rate on amount outstanding balance and interest of ₹1,59,252/- from D.S.M. Infosystems P. Ltd worked out 0.76% on the outstanding balance and there was no income from other group concerns. The Assessing Officer has made a comparison that the assessee company is paying interest at a higher rate than the interest received from its group concerns. So with these parameters of application of loan funds from group concerns and also not charging interest made in subsidiary concerns. The Assessing Officer analyzed based on the financial statements that the assessee company has obtained loans from bank, directors, shareholders and others and paying higher rate of interest wereas no interest income was received from subsidiaries except concessional rate of interest receipt from DSM Geodata Ltd and DSM infosystems P. Ltd and issued show cause notice to the assessee company for proportionate disallowance of interest on borrowed funds. In response to show cause notice, the ld. Authorised Representative filed detailed submissions and also relied on the decision of Co-ordinate Bench Tribunal in assessee's own case for the assessment

year 2004-05 and 2005-06 were the Tribunal has accepted the contention that the loans and advance to the group concerns or subsidiaries is for commercial expediency and no interest disallowance is warranted on such investments in subsidiaries. The ld. Assessing Officer perused the Tribunal order and found the Department has not accepted the decision of the Tribunal and contesting at higher forum in High Court. The ld. Assessing Officer has not relied on the decision and calculated proportionate disallowance of interest on the advance made to group concerns and worked out the calculation of interest component in is order and disallowed ₹58,87,623/-. Aggrieved by the order, the assessee filed an appeal before the Commissioner of Income Tax (Appeals).

4. In the appellate proceedings, the ld. Authorised Representative made submissions on disallowance and the assessee company has advanced and invested in the subsidiary companies. The ld. Assessing Officer without considering the provisions of Sec. 36(1)(iii) of the Act on the borrowed funds and decision of Tribunal made disallowance. The ld. Commissioner of Income Tax (Appeals) considered the submissions of the assessee and observed the findings of the Assessing Officer on similar issue, the ITAT decision in assessee's own case for assessment year 2004-05 and 2005-06 observed at para 5.1 of his order as under:-

''I have carefully considered the facts, order of the AO, submissions of the appellant and material on record. The ITAT order arising from cross appeals in ITA Nos.11 & 12/Mds/2010 for the A.Ys 2004-05 and 2005-06 as also ITA Nos.366 & 367/Mds/2010 relied upon in the appellant's own case has been carefully perused by me. The facts obtaining therein related to disallowance of interest on borrowed capital. These related to interest-free advance or advance on nominal rates of (i) ₹1 crore given to its group concern M/s Morgan Industries Ltd., (ii) Rs.49.14 lakhs to another group concern M/s DSM Infosystems P Ltd, (iii) besides net advance of ₹1,54,52,372/- to another group company M/s DSM Geodata Ltd. The appellant had during the relevant previous year borrowed fresh loan of ₹.2.65 crores. The ITAT on the pleas made by the appellant had observed after taking into consideration the findings of the CIT(A) in this matter, that the assessee had used interest free funds as advances to the three companies mentioned above besides making investment in equity shares of the subsidiary Mls DSM Geodata Ltd. The ITAT held that the loans were given by the assessee to the companies on account of commercial expediency and that revenue , could not bring any evidence on record to show that amounts advanced or invested were used for personal benefit I purpose. In a speaking order, the Hon'bie ITAT deleted the disallowance made by the AO on account of interest in relation to the loans given by it to its group concerns and investments made in equity shares in its subsidiary company. Respectfully following the decision of the Hon'ble ITAT and having regard to the fact that the matter is identical in the year under consideration in appeal, I hold that the disallowance made by the AO cannot be upheld and direct the AO to delete the disallowance thus made. The ground is allowed.''

The ld. CIT(A) following the ITAT decision allowed the appeal of the assessee. Aggrieved by the order of the Commissioner of Income Tax (Appeals), the Revenue has assailed an appeal before Tribunal.

5. Before us, the ld. Departmental Representative reiterated the findings of the Assessing Officer, the Commissioner of Income Tax (Appeals) has deleted the disallowance of interest on borrowed capital utilized for group concerns and relied on the Supreme Court decision

without considering the fact that the Revenue has not accepted the decision relied by the Commissioner of Income Tax (Appeals) in assessee's own case for earlier assessment years and appeal has been filed in High Court and prayed for setting aside the Commissioner of Income Tax (Appeals) order.

6. Contra, the ld. Authorised Representative of the assessee made submissions and relied on the order of Commissioner of Income Tax (Appeals) and decision of ITAT in assessee's own case for the assessment years 2004-05 and 2005-06 where the Tribunal has allowed the appeal in favour of the assessee.

7. We heard the rival submissions, perused the material on record and judicial decisions cited. The ld. Departmental Representative contested the issues that the Commissioner of Income Tax (Appeals) has not considered the facts on the borrowed capital and investment in equity of subsidiary companies and applied the decision of Apex Court and also Tribunal decision which has not attained finality for earlier assessment years as Department has contested the issue at higher forum. This Tribunal is of the considered opinion that mere pendency of appeal before the higher forum cannot be a reason to take a different view. So respectfully following the

decision in assessee's own in ITA Nos.11 & 12/Mds/2010 and ITA Nos.366 & 367/MDS/2010 upheld the order of the Commissioner of Income Tax (Appeals) and dismiss the ground of the Revenue.

8. The second ground raised by the Department that Commissioner of Income Tax (Appeals) has deleted the disallowance u/s.40(a)(i) of the Act on Software expenses without appreciating the legal fiction as per the Finance Act, 2012.

9. The ld. Assessing Officer on perusal found that an amount of ₹44,85,800/- was paid to software maintenance to M/s. Bentley Systems. The ld. Authorised Representative filed detailed explanations and clarifying that the amount paid to the M/s. Bentley Systems towards subscription/annual license fee for providing services such as geographic information systems and engineering and not any purchase of asset. This payment is in the nature of subscription but the ld. Assessing Officer has assumed that the payment is made for specialized services in the nature of technical services and knowhow for the usage of the product where the provisions of Sec.195 are applicable. The assessee submitted that software is used for providing services to client outside India and as per Sec.9(1)(vi)(b) shall not fall under the category of royalty payments were TDS provisions apply. The ld. Assessing Officer found that explanations are not satisfactory

and fall under the category of royalty and technical knowhow and usage outside India cannot be a ground as the payments are made outside India having license fee for the use of software. The ld. AO categorized payments as royalty and relied on the decision of *Gracemac Corp. vs. ACIT, 134 TTJ 257* were payments of royalty of nonresident is deemed to accrue or arise in India irrespective of the fact whether non resident has a residence or place of business in India and concludes that the provisions of TDS shall comply and made disallowance u/s.40(a)(i) of the Act of ₹44,85,800/-. Aggrieved by the order, the assessee filed an appeal before the Commissioner of Income Tax (Appeals).

10. In the appellate proceedings, the Commissioner of Income Tax (Appeals) considered the grounds, submissions of the assessee and also findings of the Assessing Officer were an amount of ₹44,85,800/- paid by the assessee to M/s. Bentley Systems, a resident of Australia. The ld. Commissioner of Income Tax (Appeals) considered the submissions of the assessee and observed the findings of the Assessing Officer and relied on jurisdictional ITAT decision *Financial Software Services P. Ltd vs. DCIT 47 taxman.com 410* at page 6 para 6.2 of the order as under and allowed the ground

> *'I have carefully considered the facts of the case, order of the AO, submissions made by the appellant and material on record. The appellant is engaged in business of software development*

and export. It operates also through its own subsidiary and associate companies DSM Geodata Ltd, Scotland, DSM Infosystems P Ltd and DSM BPO P Ltd. For the purposes of its business it is required to use a software on a year to year basis. The software is used to offer services to its client overseas. The software in question has been licensed for use by Mls Bentley Systems Pty Ltd, an non- resident. From the options available, the appellant has opted to pay certain price for each licence for the user of the software. It is also possible that the appellant would have to pay such licence fee for each of those applications as and when the need arises. The second option available to the appellant was to obtain enterprise licences for a year at different price whereby it had the option of using as many licences as it wants and also use the other applications of Bentley within the same price. In this option the appellant was required to pay a lump sum amount to the supplier of the application. Based on prudence, the appellant opted for the second option.

6.2.1 Be that as it may the tax invoice raised by the supplier of the software acknowledges payment towards licence fee for the use of such software. The provisions of s.9(1)(vi) provides through a deeming provision income to accrue or arise in India and includes income by way of royalty. Explanation 2 further defines royalty for use or right to use any industrial commercial or scientific equipment. Explanation 4 further clarifies that transfer of all or any rights in respect of any right, property or information includes and as always included transfer of all or any right for use or right to use a computer software, including granting of a licence, irrespective of the medium through which such right is transferred. The explanation inserted by Finance Act, 2012 is with retrospective effect from 1.6.1976. As the explanation suggests it is clarificatory in nature and does not substantively legislate on a new item of income. In my considered view, from the facts obtaining in this case the consideration paid to M/s Bentley Systems Pty Ltd, a non-resident, for use of the impugned software would constitute payment in the nature of royalty u/s 9(1)(vi) r.w. Article 12(3) of the DT AA with Australia attracting withholding tax u/s 195. Further, the taxability of royalty in the source state does not depend on, unlike the taxability in the resident state to whom the royalties are paid. These are taxed according to the domestic laws. In India income is taxable on receipt or cash basis but also on accrual basis. Thus, when an income is credited to foreign company, it becomes taxable and tax is required to be deducted in terms of s. 195(1) of the I.T. Act. The order of the AO does not suffer any infirmity. However, notwithstanding the same and having respect to the plea of the

appellant and reliance placed in the ratio of the jurisdictional bench of ITAT in the case of Financial Software Services P Ltd (supra), I hold that the plea taken by the appellant must succeed. This ground of appeal is allowed".

Aggrieved by the order of the Commissioner of Income Tax (Appeals), the Revenue has assailed an appeal before Tribunal.

11. Before us, the ld. Departmental Representative reiterated the findings of the Assessing Officer and vehemently argued that the Revenue has not accepted the decision relied by the Commissioner of Income Tax (Appeals) and appeal has been filed in High Court and prayed for setting aside the Commissioner of Income Tax (Appeals) order.

12. Contra, the ld. Authorised Representative of the assessee made his submissions and relied on the order of Commissioner of Income Tax (Appeals) and decision of the ITAT.

13. We heard the rival submissions, perused the material on record and judicial decisions cited. The ld. Departmental Representative contested that the Tribunal decision has not attained finality for earlier assessment years as Department has contested the issue at higher forum. This Tribunal is of the considered opinion that mere pendency of appeal before the higher forum cannot be a reason

to take a different view. So respectfully following the decision in *Financial Software & Systems (P) Ltd in ITA Nos.2190 to 2196 & 2199/Mds/2013* upheld the order of the Commissioner of Income Tax (Appeals) and dismiss the ground of the Revenue.

14. The Department has raised third ground where the Commissioner of Income Tax (Appeals) erred in holding that business losses of a unit cannot be set off against profit undertaking eligible for deduction u/s.10A of the Act and allowed the same.

15. The assessee during the financial year 2007-08 derived income from export operations and domestic operations. The ld. Assessing Officer on perusal of the computation of income found that the assessee has claimed exemption of ₹1,09,85,430/- as exempted income u/s.10A and at the same time assessee has loss from the domestic operations ₹57,16,767/- and claimed to be carried to subsequent years. The main dispute arise with respect of claim of deduction u/s.10A on profit of export operation without set off loss from domestic operations. The ld. Assessing Officer referred to the amendment u/s.10A effective from 01.04.2001 available only to the total income of the assessee with prospective to provisions in adjustment of loss with profit of export unit. The ld. Authorised

Representative submitted the details and also supported his submissions with decisions in assessee own case by Tribunal for the assessment year 2007-08 were the Tribunal has allowed the deduction u/s.10A of the Act. The entire profits of STPI units without setting off of the loss of non –STPI units. But the Assessing Officer considered though the Tribunal has accepted the assessee's contention but the Department has contested the Tribunal order of the assessee at higher forum to keep the issue alive, the ld. Assessing Officer deferred the decision of assessee's own case and made that elaborate findings on the provisions were the Tribunal relied on the Special Bench decision in the case of *Scientific Atlanta Technology Pvt. Ltd vs. ACIT 129 TTJ 273* and the Department is contesting the decision of Special Bench at higher forum. Considering both the decisions contested by the Department, the Assessing Officer discussed the provisions applicable for claiming deduction u/s.10A effective from 01.04.2001 and made a elaborate submissions and relied on the Tribunal decision and distinguished the Tribunal order. The computation of u/s.10A deduction shall be worked out in the manner laid down in the Act and application of provisions of Secs.70 and 72 of the Act. The deduction u/s.10A has to be allowed only after adjustment of loss of domestic unit with profits of the EOU and made addition and disallowed excess

claim of the assessee. Aggrieved by the order, the assessee filed an appeal before the Tribunal.

16. In the appellate proceedings, the ld. Authorised Representative reiterated his submissions made in the assessment proceeding. The ld. Assessing Officer has not accepted the assessee contention for claim of deduction u/s.10A and also the Tribunal order applicable to assessee's own case for the assessment year 2007-08 and the Assessing Officer further made a distinction based on the provisions applicable and also Department has not accepted the decision and contesting in higher forum and relied on the decision of the Tribunal irrespective of the fact that Commissioner of Income Tax (Appeals) and Tribunal in assessee's own case allowed based on the Special Bench decision of ITAT, Chennai in *Scientific Atlanta India Technology P. Ltd vs. ACIT 129 TTJ 273*. The ld. Commissioner of Income Tax (Appeals) considering the grounds submissions of the Authorised Representative and also findings of the Assessing Officer has allowed the ground of the assessee observing at 8.2 of the order as under:-

> "I have carefully considered the facts, order of the Assessing Officer, submissions made by the appellant and material on record. The ITAT order in ITA No.890/Mds/2010 for the A.Y. 2007-08 relied upon in the appellant's own case has been carefully perused by me. The Hon'ble ITAT has held as under:-

> *5. We have perused the order and heard the parties. In view of the decision of the Special Bench of this Tribunal in the case of Scientific Atlanta Technology P. Ltd (supra), reproduced by the ld.CIT(A) at paras 5 and 5.1 of his order, the assessee was well eligible for claiming deduction for its unit on which Sec.10A claim was allowable, without setting off of the losses of its domestic unit."*

Aggrieved by the order of the Commissioner of Income Tax (Appeals), the Revenue assailed an appeal before the Tribunal.

17. The ld. Departmental Representative relied on the order of the Assessing Officer and vehemently argued for allowing the appeal.

18. Contra, the ld. Authorised Representative of the assessee relied on the order of Commissioner of Income Tax (Appeals) and Tribunal decision in assessee's own case, prayed for dismissing the appeal.

19. We heard the rival submissions, perused the material on record and judicial decisions cited. The ld. Departmental Representative explained that the ITAT decision has not attained finality and being contested at higher forums. The Commissioner of Income Tax (Appeals) has allowed the ground of the assessee based on assessee's earlier year order relying on the Special Bench decision of *Scientific Atlanta Technology Pvt. Ltd (Supra)* were deduction u/s.10A of the Act was allowed without setting off of loss of domestic

unit. The decision of the Tribunal was based on prevailing law and we know rely on the decision of Madras High Court in the case of *CIT vs. Hi Tech Arai Ltd 321 ITR 477* where it was held ‘’that merely because a Co-ordinate Bench of the Tribunal had earlier taken a different view, the Tribunal need not blindly follow the earlier decision even if the earlier decision did not reflect the correct position of law’’. The claim of deduction u/s. 10A should be considered based on the amendment effective from 01.04.2001 were the deduction in respect of profit and gains determined for eligible industrial undertaking for export of articles or things. The Profit and gains from eligible undertaking calculated in proportion of export turnover to total turnover and allowed as deduction while computing the taxable income only to the extent of income from such undertaking as included in the total income. Consequently, the Deduction would be worked out on the total income of the assessee, and arrived after set-off of the profit from export division against loss of the other unit/business, if any, as per Sec.70 & 72 of the Income Tax Act. So, considering the provisions of law, Amendment and decision of Madras High Court, we rely on the decision of Delhi High Court in the case *of CIT vs. KEI Industries Ltd 373 ITR 574* were loss of a unit entitled for exemption not to be set off against income from unit not eligible for such exemption. The

lordship has referred the cases which were relied by the ld. Authorised Representative. The question of set off of loss under provisions of section 10B of the Act has same parameters for deduction under Sec. 10A of the Act. The loss of EOU unit cannot be set off against business income of non EOU unit by applying the ratio to the present case, gives a ray of adjustment to circumstances were EOU unit has profit and non EOU has losses. On the same analogy of facts and ratio, we find that the ld. Commissioner of Income Tax (Appeals) has allowed the claim of the assessee without set off of loss of domestic operations, relying on earlier year order is not correct. We are of the opinion that claim of deduction u/s.10A is allowable after set off of losses in accordance with the provisions of Sec. 70 & 72 of the Act and the deduction of 10A has to be considered only after set off of losses of domestic operations. Therefore, we direct the Assessing Officer to allow the deduction u/s.10A of the Act after set off adjustment of losses of domestic operations with the income of export operations. This ground of the Revenue is allowed.

20. In the result, the appeal of the Revenue in ITA No.2059/Mds/2015 for the assessment year 2008-09 is partly allowed and Revenue appeal in ITA No.2062/Mds/2015 for the assessment

year 2009-2010 is also dismissed.

Order pronounced on Wednesday, the 30th day of March, 2016, at Chennai.

Sd/-	Sd/-
(चंद्र पूजारी)	**(जी. पवन कुमार)**
(CHANDRA POOJARI)	**(G. PAVAN KUMAR)**
लेखा सदस्य /ACCOUNTANT MEMBER	**न्यायिक सदस्य/JUDICIAL MEMBER**

चेन्नई/Chennai
दिनांक/Dated:30.03. 2016
KV

आदेश की प्रतिलिपि अग्रेषित/Copy to:

1. अपीलार्थी/Appellant	3. आयकर आयुक्त (अपील)/CIT(A)	5. विभागीय प्रतिनिधि/DR
2. प्रत्यर्थी/Respondent	4. आयकर आयुक्त/CIT	6. गार्ड फाईल/GF