IN THE INCOME TAX APPELLATE TRIBUNAL

"K" BENCH, MUMBAI

BEFORE SHRI SAKTIJIT DEY, JUDICIAL MEMBER AND

SHRI ASHWANI TANEJA, ACCOUNTANT MEMBER

ITA no.641/Mum./2007
(Assessment Year : 2003–04)

Strides Shasun Limited
(Formerly known as Strides Arolab Ltd.)
201, Devavrata, Sector–17 ……. Appellant
Vashi, Navi Mumbai 400 703
PAN – AADCS8104P

v/s

Income Tax Officer
Ward–10(3)(4), Aayakar Bhawan ……. Respondent
101, M.K. Road, Mumbai 400 020

ITA no.4063/Mum./2010
(Assessment Year : 2004–05)

Asstt. Commissioner of Income Tax
Range–10(1), Aayakar Bhawan ……. Appellant
101, M.K. Road, Mumbai 400 020

v/s

Strides Arcolab Limited
201, Devavrata, Sector–17
Vashi, Navi Mumbai 400 703 ……. Respondent
PAN – AADCS8104P

C.O. no.61/Mum./2010
(Arising out of ITA no.4063/Mum./2010)
(Assessment Year : 2004–05)

Strides Arcolab Limited
201, Devavrata, Sector–17
Vashi, Navi Mumbai 400 703
PAN – AADCS8104P

……. Appellant
(Original Respondent)

v/s

Dy. Commissioner of Income Tax
[Earlier Income Tax Officer
Ward–10(3)(4)], Circle–15(3)(2)
Aayakar Bhawan, 101, M.K. Road
Mumbai 400 020

……. Respondent
(Original Appellant)

ITA no.274/Mum./2007
(Assessment Year : 2003–04)

Income Tax Officer
Ward–10(3)(4), Aayakar Bhawan
101, M.K. Road, Mumbai 400 020

……. Appellant

v/s

Strides Arcolab Limited
201, Devavrata, Sector–17
Vashi, Navi Mumbai 400 703
PAN – AADCS8104P

……. Respondent

C.O. no.121/Mum./2007
(Arising out of ITA no.274/Mum./2007)
(Assessment Year : 2003–04)

Strides Arcolab Limited
201, Devavrata, Sector–17
Vashi, Navi Mumbai 400 703
PAN – AADCS8104P

……. Appellant
(Original Respondent)

v/s

Income Tax Officer
Ward–10(3)(4), Aayakar Bhawan
101, M.K. Road, Mumbai 400 020

……. Respondent
(Original Appellant)

Assessee by : Shri Nitesh Joshi
Revenue by : Shri N.K. Chand

Date of Hearing – 15.03.2016	Date of Order – 29.04.2016

O R D E R

PER BENCH

Cross appeals by the assessee & the Department and cross objection by the assessee for the assessment year 2003–04 and appeal by the Department and cross objection by the assessee for the assessment year 2004–05, are directed against separate orders of the learned Commissioner (Appeals)–10, Mumbai.

2. As these cross appeal and cross objection pertain to the same assessee and involve common issues arising out of materially similar set of facts and circumstances, they were heard together and as a matter of convenience, therefore, all the cross appeals / cross objection are being disposed off by way of this consolidated order.

ITA no.641/Mum./2007 – Assessee's Appeal

Assessee has raised five grounds in this appeal.

3. Ground no.1, relates to disallowance of assessee's claim of deduction under section 35(2AB) of the Income Tax Act, 1961 (for short *"the Act"*) amounting to ₹ 1,61,96,892.

4. Brief facts relating to this issue are assessee company filed its return of income for the impugned assessment year on 1st December 2003, declaring loss of ₹ 3,15,35,060, under the normal provisions and paid tax of ₹ 5,44,980 under section 115JB of the Act. Subsequently, assessee on 31st March 2005, filed a revised return of income declaring loss of ₹ 5,25,97,009, under the normal provisions and computed tax of ₹ 1,09,148, on the book profit declared under section 115JB. During the assessment proceedings, the Assessing Officer noticed that

assessee had debited an amount of ₹ 3,23,93,782 to the Profit & Loss account on account of research and development expenditure and claimed deduction under section 35(2AB) for an amount of ₹ 4,85,90,676. When called upon by the Assessing Officer to justify the deduction claimed with supporting evidence, it was submitted by the assessee that the expenditure of ₹ 3,23,93,782, was incurred during the relevant previous year. He submitted, as the expenditure incurred was on research and development the same is allowable under section 35(2AB). It was further stated, though, he assessee filed an application before the prescribed authority, it is still pending for approval. The Assessing Officer being of the opinion that without approval from prescribed authority i.e., Department of Scientific and Industrial Research (DSIR), deduction under section 35(2AB) cannot be allowed and as the assessee has failed to produce copy of the agreement entered with the prescribed authority, no deduction under section 35(2AB) can be allowed. Accordingly, the Assessing Officer disallowed excess deduction claimed at 150% amounting to ₹ 1,61,96,892. Being aggrieved of such disallowance, assessee preferred appeal before the learned Commissioner (Appeals).

5. The learned Commissioner (Appeals) also sustained the disallowance by concurring with the findings of the Assessing Officer.

6. Before us, learned Authorised Representative submitted, the issue is covered in favour of the assessee by the decision of the Tribunal in assessee's own case for the assessment year 2002–03. In this context, he referred to the observations of the Tribunal in ITA no.1727/Mum./2006 dated 16th December 2015.

7. Learned Departmental Representative, without controverting the fact that similar issue was decided in assessee's own case by the Tribunal, preferred to rely upon the observation of the Assessing Officer and the learned Commissioner (Appeals).

8. We have considered the submissions of the parties and perused the material available on record. As could be seen from the facts on record, the Assessing Officer has not disputed that assessee has incurred the expenditure of ₹ 3,23,93,782. The dispute is with regard to assessee's claim of deduction under section 35(2AB) @ 150% of the expenditure incurred. The Assessing Officer, though, has allowed the actual expenditure incurred by the assessee on research and development, he has disallowed weighted deduction @ 150% on the ground that assessee has failed to furnish copy of agreement with the prescribed authority. It is noticed by us that similar issue arose in assessee's own case in assessment year 2002–03 and the Tribunal after considering the submissions of the parties vis–a–vis deduction claimed under section 35(2AB), held as under:–

> *"3.4. We have gone through the submissions made by both the sides as well as facts of the case and the position of law emerging out from the decisions relied upon by the parties before us. The brief facts are that deduction u/s 35(2AB) was claimed by the assessee in respect of research and development expenses incurred at New Mangalore and KRS Gardens research centre. Application was made with DSIR dated 28.03.2001, copy of which is enclosed at pages 37 to 68 of the paper book. The recognition of the research unit was granted by the DSIR vide its letter dated 03.07.2002 for New Mangalore unit (copy available at P.B. 68) and letter dated 04.12.2002 for KRS Gardens research unit (copy available at page no.69 of the paper book). In view of these facts, it clearly emerges out that assessee had made the applications well in time. Thereafter, granting of approval by the competent authority was not in the control of the assessee. It has been further brought to our notice that there was no delay*

on the part of the assessee in supplying any information to the approval authority, if and when asked by it. In other words, the delay, in the given facts, cannot be attributed to the assessee. In fact, the assessee had no say in this regard. It is further noted by us that the approval has been granted by the competent authority after taking the application of the assessee as a base. In our considered view, under these circumstances, the approval would relate back to the date of the application. In other words, under these circumstances, it can be taken as if the approval was granted on 28.03.2001 i.e. the date of application made by the assessee. Thus, in our view, the grievance raised by the Revenue on this issue is not sustainable. It is further noted by us that this issue is no more res-integra. We can take help of judgment of Hon'ble Delhi High Court in the case of CIT vs. Sandan Vikas (India), (supra) wherein their lordships have held, following the judgments of Hon'ble Gujarat High Court in the case of CIT vs. Claris Lifesciences Ltd. (supra), that assessee would be eligible for deduction even if the approval is granted by the competent authority subsequent to the expiry of the previous year. The relevant portion of the judgment is reproduced below:

> *"The Assessing Officer, however, refused to accord the benefit of the aforesaid provisions of weighted deduction to the assessee on the ground that recognition and approval was given by the DSIR in February/September 2006, i.e., in the next assessment year and, therefore, the assessee was not entitled to the benefit. The CIT(Appeal) accepted this view of the Assessing Officer and dismissed the appeal, however, the Income Tax Appellate Tribunal (hereinafter referred to as "the Tribunal") has come to the conclusion that the assessee would be entitled to weighted deductions of the aforesaid expenditure incurred by the assessee in terms of the Section 35(2AB) of the Act and in coming to this conclusion, the Tribunal has relied upon the judgment of Gujarat High Court in Commissioner of Income Tax v. Claris Lifesciences Ltd., 326 ITR 251(Guj). We have gone through the aforesaid judgment of the Gujarat High Court and find that Gujarat High Court detailed in nouncertain terms that the cut-off date mentioned in the certificate issued by the DSIR would be of no relevance. What is to be seen is that the assessee was in indulging in R&D activity and had incurred the expenditure thereupon. Once a certificate by DSIR is issued, that would be sufficient to hold that the*

assessee fulfils the conditions laid down in the aforesaid provisions. The discussion, which is undertaken by the Gujarat High Court while interpreting the aforesaid provisions, is extracted below:

> *"7. .....The lower authorities are reading more than what is provided by law. A plain and simple reading of the Act provides that on approval of the research and development facility, expenditure so incurred is eligible for weighted deduction.*
>
> *8. The Tribunal has considered the submissions made on behalf of the assessee and took the view that section speaks of:*
>
> *(i) development of facility;*
>
> *(ii) incurring of expenditure by the assessee for development of such facility;*
>
> *(iii) approval of the facility by the prescribed authority, which is DSIR; and*
>
> *(iv) allowance of weighted deduction on the expenditure so incurred by the assessee.*
>
> *9. The provisions nowhere suggest or imply that research and development facility is to be approved from a particular date and, in other words, it is nowhere suggested that date of approval only will be cut-off date for eligibility of weighted deduction on the expenses incurred from that date onwards. A plain reading clearly manifests that the assessee has to develop facility, which presupposes incurring expenditure in this behalf, application to the prescribed authority, who after following proper procedure will approve the facility or otherwise and the assessee will be entitled to weighted deduction of any and all expenditure so incurred. The Tribunal has, therefore, come to the conclusion that on plain reading of section itself, the assessee is entitled to weighted deduction on*

expenditure so incurred by the assessee for development of facility. The Tribunal has also considered Rule 6(5A) and Form No. 3CM and come to the conclusion that a plain and harmonious reading of Rule and Form clearly suggests that once facility is approved, the entire expenditure so incurred on development of R&D facility has to be allowed for weighted deduction as provided by Section 35(2AB). The Tribunal has also considered the legislative intention behind above enactment and observed that to boost up research and development facility in India, the legislature has provided this provision to encourage the development of the facility by providing deduction of weighted expenditure. Since what is stated to be promoted was development of facility, intention of the legislature by making above amendment is very clear that the entire expenditure incurred by the assessee on development of facility, if approved, has to be allowed for the purpose of weighted deduction.

10. We are in full agreement with the reasoning given by the Tribunal and we are of the view that there is no scope for any other interpretation and since the approval is granted during the previous year relevant to the assessment year in question, we are of the view that the assessee is entitled to claim weighted deduction in respect of the entire expenditure incurred under Section 35(2AB) of the Act by the assessee."

3. We are in full agreement with the aforesaid approach of the Gujarat High Court. No substantial question of law, therefore, arises. The appeal is dismissed."

3.5. It is noted by us that similar view has been taken by Hon'ble Madras High Court in the case of CIT vs. Wheels India Ltd. (supra). Thus, keeping in view the clear position of law and the facts of this case, stand of the Revenue on this issue is rejected. The other issue raised by the AO in disallowing the deduction was that no agreement has been entered as

contemplated by section 35(2AB). In this regard also we have noted that the assessee has made requisite compliance as has been required by the prescribed competent authority and compliance of all the procedural requirements has been examined by the competent authority while granting approval. In our considered view, we should look substantive compliance of the provisions. Documentation in any particular format and its approval in a particular manner is not object of this action. In any case, all these aspects have been examined by the competent authority while granting approval, thus the AO should not have denied benefit of deduction on his whims and fancies. We find that the assessee has rightly placed reliance on the judgment of coordinate bench in the case of ACIT vs. Meco Instruments (supra) and Sri Biotech Laboratories India Ltd., supra, in support of his claim.

3.6. Thus, taking into accounts all the facts and circumstances of the case as well as aforesaid judgments, we find that the assessee is eligible for deduction u/s 35(2AB) and the same was wrongly denied to the assessee, and therefore, we direct the AO to grant the benefit of deduction u/s 35(2AB). Ground no.1 of the assessee's appeal is allowed."

9. In the impugned assessment year also, the disallowance of claim of deduction under section 35(2AB) by the Assessing Officer is on the basis of similar reasoning on which disallowance was made in assessment year 2002–03. Since, the Tribunal while deciding the issue has found the reasoning of the Assessing Officer unacceptable, respectfully following the view expressed by the Tribunal in assessee's own case for the preceding assessment year, we allow assessee's claim of deduction under section 35(2AB). Ground no.1, is allowed.

10. Ground no.2, is in respect of disallowance of interest of ₹ 4,92,39,106, on the ground of advance made to Indian subsidiary.

11. Brief facts are, during the assessment proceedings, the Assessing Officer found that the assessee has claimed deduction of ₹ 17.70 crores on account of interest expenditure on various credit facilities

availed by it. He also found that the assessee had made advances to Indian subsidiaries amounting to ₹ 49,23,91,0673 as under:–

Global Remedies Ltd.	*₹ 7,53,55,446*
Caryl Laboratories Ltd.	*₹ 11,01,04,498*
Strides Research and Specialties	*₹ 30,69,31,123*

12. He, therefore, called upon the assessee to explain why proportionate interest relating to advance made to the subsidiary should not be disallowed out of the interest expenditure claimed. In response to the query raised by the Assessing Officer, it was submitted by the assessee, as far as Global Remedies Ltd. and Caryl Laboratories Ltd. are concerned, the advances to them are towards conversion charges since they have a 100% dedicated plant for meeting assessee's manufacturing requirements to certain market segments. As far as advances made to Strides Research and Specialties, it was submitted, the Contract Research Manufacturing Division (CRMD) was hived off w.e.f. 1st April 2002, by virtue of a Court order and as per the scheme of arrangement framed by the Court, out of the amount of ₹ 30,69,31,123, which was appearing in the books of account. an amount of ₹ 23 crore was treated as advance and balance amount which pertains to inter division expenditure post hive off was treated as advance and required to be repaid by the subsidiary. The Assessing Officer referring to the balance sheet of the assessee observed investment in Global Remedies Ltd. and Caryl Laboratories Ltd. are to the tune of ₹ 2.61 crore and ₹ 5.09 crore respectively as on 31st March 2003. He further found, during the previous year relevant to assessment year 2003–04, assessee has made payments on account of job works to these subsidiaries to the tune of ₹ 1.26 crore and ₹ 1.01 crore respectively. On a comparative analysis, he found that the

funds advanced to the subsidiaries are nearly 6 times and 11 times of the job work charges paid. He further found that the advances are on account of various expenses incurred on behalf of subsidiary companies which have to be recovered by the assessee. The Assessing Officer was of the view that the assessee should either have recovered the same during the previous year or it should have charged interest on the same. He observed, while on one hand, assessee was incurring costs on account of interest the subsidiary is benefiting by availing interest free funds.

13. As far as Strides Research and Specialties is concerned, the Assessing Officer observed, it is a separate and distinct profit centre as the division was hived off into a separate company w.e.f. 1st April 2002. He observed, as per the scheme of arrangement, the excess of book value of asset over the liabilities as reduced by the shares allotted pursuant to the claim has been treated as amounts due to the assessee company. Therefore, the assessee should have recovered the sum during the previous year or should have charged interest on the same. The Assessing Officer also alleged that advance to Strides Research and Specialties includes funds advanced to M/s. Xlencea Products Pvt. Ltd., who in turn has advanced to four other parties who were found to have advanced funds to the assessee company in the form of share application money amounting to ₹ 2.14 crore. Thus, on the basis of the aforesaid factual analysis, the Assessing Officer concluded that the entire interest expenditure incurred by the assessee cannot be allowed under section 36(1)(iii) as the assessee has not used the borrowed funds for its own business. He observed, as the assessee was paying interest @ 10%, proportionate disallowance applying the same rate has to be worked out from the interest expenditure on

the advance made by the assessee to subsidiaries. Accordingly, he worked out the disallowance at ₹ 4,92,39,106. Being aggrieved of such disallowance, assessee preferred appeal before the first appellate authority.

14. Learned Commissioner (Appeals) also confirmed the disallowance more or less relying upon the observations of the Assessing Officer.

15. Learned Authorised Representative reiterating the stand taken before the Departmental Authorities, submitted that Global Remedies Ltd. and Caryl Laboratories Ltd., are 100% subsidiaries of the assessee and during the relevant financial year, they are having dedicated plants to meet assessee's manufacturing requirements. It was submitted, assessee paid job work, data conversion charges for suply of goods. Thus, the advances made are on the basis of commercial expediency. He further submitted, in any case of the matter, the advances made being out of interest free funds / internal accruals available with the assessee no disallowance out of interest expenditure can be made. In support of such contention, he relied upon the decision of the Hon'ble Supreme Court in Hero Cycles P. Ltd. v/s CIT, [1997] 379 ITR 347 (SC). As far as advance to Strides Research and Specialties, learned Authorised Representative submitted that assessee had demerged its CRAM division to form a separate company w.e.f. 1st April 2002, as per the directions of the Court. He submitted, pursuant to demerger, the debit balance to the CRAM division was treated as advance to the new company. Learned Authorised Representative submitted, the so called advance is a mere book entry and there was no actual cash out flow from the assessee to the said company towards such demerger. Learned Authorised Representative submitted, though, advance to Indian subsidiary companies were

made from the earlier assessment year and also continued in subsequent assessment years, the Assessing Officer has not made any disallowance up to assessment year 2002–03 or even in subsequent assessment year 2004–05 to 2006–07, though, assessments were completed under section 143(3) of the Act. He submitted, in fact in assessment year 2004–05, against the disallowance made by the Assessing Officer, assessee preferred appeal before the learned Commissioner (Appeals) accepting assessee's claim deleted the addition and Department accepted the decision of the learned Commissioner (Appeals) by not preferring any appeal before the Tribunal. He submitted, from assessment year 2005–06, the Assessing Officer himself did not make any disallowance under section 36(1)(iii). Thus, it was submitted by the assessee, no disallowance should have been made.

16. Learned Departmental Representative relying upon the reasoning of the Departmental Authorities submitted, assessee has to prove commercial expediency.

17. We have considered the submissions of the parties and perused the material available on record. Undisputedly, two of the companies to whom advances were made by the assessee viz., Global Remedies Ltd. and Caryl Laboratories Ltd. are 100% subsidiary of the assessee. It is also not disputed that these two companies have dedicated plants to only manufacture the products of the assessee. It is also borne out on record that for such manufacturing activities undertaken by these subsidiaries, assessee paid job work / conversion charges. These facts are not disputed by the Assessing Officer. Therefore, it is proved on record that there is a business relationship between the assessee and the two subsidiaries. That being the case, it cannot be said that the

advance made to these subsidiaries is not for the purpose of business. Moreover, the fact that Assessing Officer has not disallowed expenditure on advances made to the subsidiaries on the ground of commercial expediency in the earlier assessment year or subsequent assessment year has not been controverted by the Department., As far as the advance to Strides Research and Specialties is concerned, it is evident on record that there was no actual cash outflow. When the CRAM division of assessee company was hived off and the separate company was formed as per the scheme of arrangement framed by the Court, the debit balance standing in the books in the name of CRAM was treated as advance. Thus, as could be seen, the assessee has actually not made any advances to Strides Research and Specialties, in strict sense of the term. Moreover, the Department has also failed to establish nexus between the borrowed funds and advances made. One more crucial factor which cannot be ignored is, though, similar advances have been made to the Indian subsidiary in preceding as well as subsequent assessment years, the Assessing Officer has never disallowed proportionate interest expenditure, even though, assessments have regularly been completed under section 143(3) of the Act. In fact, in assessment year 2004–05, the disallowance made by the Assessing Officer on the ground of commercial expediency was found unacceptable by the learned Commissioner (Appeals) and the Department accepted the decision of the learned Commissioner (Appeals) by not referring any further appeal. All these facts invariably prove that the advances made are on account of commercial expediency as the assessee has a close business connection with the subsidiaries. The Hon'ble Supreme Court in Hero Cycle Ltd. (supra), while approving its earlier decision in CIT v/s S.A. Builders, [2007] 288 ITR 001 (SC) held as under:–

"12. Insofar as loans to the sister concern/subsidiary company are concerned, law in this behalf is recapitulated by this Court in the case of S.A. Builders Ltd. v. CIT (Appeals) [2007 (288) ITR 1/158 Taxman 74]. After taking note of and discussing on the scope of commercial expediency, the Court summed up the legal position in the following manner:—

> *'26. The expression "commercial expediency" is an expression of wide import and includes such expenditure as a prudent businessman incurs for the purpose of business. The expenditure may not have been incurred under any legal obligation, but yet it is allowable as a business expenditure if it was incurred on grounds of commercial expediency.*
>
> *27. No doubt, as held in Madhav Prasad Jatia v. CIT [1979 (118) ITR 200 (SC)], if the borrowed amount was donated for some sentimental or personal reasons and not on the ground of commercial expediency, the interest thereon could not have been allowed under section 36(1)(iii) of the Act. In Madhav Prasad's case [1979 (118) ITR 200 (SC)], the borrowed amount was donated to a college with a view to commemorate the memory of the assessee's deceased husband after whom the college was to be named, it was held by this court that the interest on the borrowed fund in such a case could not be allowed, as it could not be said that it was for commercial expediency.*
>
> *28. Thus, the ratio of Madhav Prasad Jatia's case [1979 (118) ITR 200 (SC)] is that the borrowed fund advanced to a third party should be for commercial expediency if it is sought to be allowed under section 36(1)(iii) of the Act.*
>
> *29. In the present case, neither the High Court nor the Tribunal nor other authorities have examined whether the amount advanced to the sister concern was by way of commercial expediency.*
>
> *30. It has been repeatedly held by this court that the expression "for the purpose of business" is wider in scope than the expression "for the purpose of earning profits" vide CIT v. Malayalam Plantations Ltd. [1964 53 ITR 140 (SC), CIT v. Birla Cotton*

> *Spinning and Weaving Mills Ltd. [1971 82ITR 166 (SC)], etc.'*
>
> *13. In the process, the Court also agreed that the view taken by the Delhi High Court in CIT v. Dalmia Cement (P.) Ltd. [2002] 254 ITR 377/121 Taxman 706 wherein the High Court had held that once it is established that there is nexus between the expenditure and the purpose of business (which need not necessarily be the business of the assessee itself), the Revenue cannot justifiably claim to put itself in the arm-chair of the businessman or in the position of the Board of Directors and assume the role to decide how much is reasonable expenditure having regard to the circumstances of the case. It further held that no businessman can be compelled to maximize his profit and that the income tax authorities must put themselves in the shoes of the assessee and see how a prudent businessman would act. The authorities must not look at the matter from their own view point but that of a prudent businessman."*

18. The principle laid by the Hon'ble Supreme Court squarely applies to the facts of the present case. In view of the aforesaid, we hold that as the advance made to the subsidiary are on account of commercial business / business expediency, proportionate disallowance out of interest expenditure cannot be made. Ground no.2, is allowed.

19. Ground no.3, assessee has challenged the disallowance of ₹ 16,82,953, and ₹ 10,888, on account of PF and ESIC respectively.

20. Brief facts are, during the assessment proceedings, the Assessing Officer on a perusal of tax audit report found that there was a delay in remittance of employer's and employees' contribution to P.F. He also found similar delay in respect of payment of ESIC dues. He, therefore, called upon the assessee to explain why the expenditure incurred should not be disallowed under section 43B, and treated as assessee's income in terms of section 2(24)(x) r/w section 36(1)(va). In response to the query raised by the Assessing Officer, it was

submitted by the assessee that payments were made within the grace period and further it was submitted as the payments were made before the due date of filing of return of income for the assessment year under consideration, no disallowance under section 43B, can be made after deletion of second proviso to the said provisions.

21. The Assessing Officer, however, did not find merit in the submissions of the assessee. Relying upon certain judicial pronouncements, the Assessing Officer held that in terms of section 36(1)(va), due date as provided under the relevant provisions would mean the due date prescribed under the relevant statute and not Income Tax Act, 1961. On the aforesaid premise, he disallowed ₹ 55,20,655 and ₹ 48,89,235 under section 43B and section 36(1)(va). Being aggrieved of such disallowance, assessee preferred appeal before the first appellate authority.

22. Learned Commissioner (Appeals), after considering the submissions of the assessee in the light of certain judicial pronouncements held that employer's contribution to PF having been paid prior to date of filing of return of income is allowable. As far as employees' contribution is concerned, the learned Commissioner (Appeals) held that only if the amount was paid within the grace period provided under the relevant Act, the deduction is allowable. Accordingly, he directed the Assessing Officer to verify and compute the disallowance.

23. Learned Authorised Representative submitted, the issue is covered by the decision of the Tribunal in assessee's own case for the assessment year 2002–03.

24. Learned Departmental Representative, though, did not dispute the contention of the assessee that issue is covered by the decision of the Tribunal but he nevertheless supported the reasoning of the learned Commissioner (Appeals).

25. We have considered the submissions of the parties and perused the material available on record. As could be seen, the issue in dispute is whether the employees' and employer's contribution to PF and ESIC are allowable deduction in case it is paid beyond the prescribed date under the relevant statute but before the due date of filing of return of income under the Income Tax Act, 1961. It is observed, identical issue arose in assessee's own case for the assessment year 2002–03, in ITA no.1727/Mum./2006 dated 16th December 2015, the Tribunal, after following its own decision in assessee's case for assessment year 2001–02, allowed assessee's claim with the following observations:–

> *"5.2. We have gone through the facts of the case. The undisputed facts are that the entire payment has been made before the due date of filing the return. Similar issue came before the Tribunal in assessee's own case for A.Y. 2001-02, wherein Hon'ble Tribunal has allowed relief to the assessee, relevant para of the Tribunal's order is reproduced below:*
>
> > *"6. After considering the rival submissions and perusing the relevant material on record we find that the Hon'ble Supreme Court in the case of CIT v. Alom Extrusions Ltd. [(2009) 319 ITR 306 (SC)] has held that the amendment to first proviso and the omission of the second proviso to section 43B by the Finance Act, 2003 is retrospective. In that view of the matter any amount referred to in section 43B, being the sum payable by the employer shall be allowed as deduction if it is paid before the due date of filing of the return. The Hon'ble Delhi High Court in the case of CIT v. Aimil Ltd. [(2010) 321 ITR 508 (Del.)] has held that if employees' share is deposited before the due date then no disallowance is called for. In reaching this conclusion, the Hon'ble Delhi High Court*

> *relied on the judgment of the Hon'ble Supreme Court in the case of CIT v. Vinay Cement Ltd. [(2007) 213 CTR (SC) 268] in which it was held that the amount of employees contribution etc. deposited before the filing of return, cannot be disallowed u/s 43B. In view of the above discussion, the grievance of the assessee is accepted and objection of the Revenue is overruled."*
>
> *5.3. It is noted from the above, the Tribunal has relied upon the judgment of Hon'ble Supreme Court in the case of Alom Extrusions Ltd. and Vinay Cement Ltd. for allowing relief to the assessee. Respectfully following these judgments and the judgments of Tribunal in assessee's own case, we delete the disallowance made in this regard. Accordingly ground no.3 of assessee's appeal is allowed."*

26. Facts being identical, respectfully following the aforesaid decision of the co–ordinate bench, we allow assessee's claim of deduction in respect of payment made towards PF contribution and ESIC. This ground is allowed.

27. The issue raised in ground no.4, relates to disallowance of assessee's claim of deduction in respect of DEPB credit under section 80HHC of the Act.

28. Brief facts are, the Assessing Officer noticing that the assessee has claimed deduction under section 80HHC, in respect of sale of DEPB credits called upon the assessee to justify the same. In response to the query raised, it was submitted by the assessee, the transfer of credits under the DEPB has not resulted in any profit, hence, no amount is deductible under section 28(iiid) of the Act. It was submitted by the assessee, it had incurred losses on sale of DEPB credits amounting to ₹ 51,59,166. It was contended as the assessee had incurred losses on sale of DEPB credit, there are no amount of profit in terms of section 28(iiid), hence, assessee did not exercise

option to chose between duty draw back or DEPB rates of differences. The Assessing Officer, however, was not convinced with the reply of assessee. He was of the view that whatever amount received on transfer of DEPB credit, when credited to the Profit & Loss account, has to be treated as profit as per section 28(iiid). He, therefore, concluded that as the assessee has received ₹ 6,04,98,305, on transfer of DEPB licence, but has credit the amount of ₹ 5,17,53,249, 90% of the said amount is to be reduced from profit of business for computing deduction under section 80HHC. Being aggrieved of such disallowance of deduction under section 80HHC, assessee preferred appeal before the learned Commissioner (Appeals).

29. Learned Commissioner (Appeals) after considering the submissions of the assessee that only profit on transfer of DEPB credit is covered by the newly inserted section 28(iiid), however, did not accept the same and confirmed the assessment order on this issue.

30. Learned Authorised Representative submitted, the face value of DEPB credit during the year was ₹ 6,56,57,201, whereas, the assessee sold such credit at net value of ₹ 6,04,98,035, thereby incurred a loss of ₹ 51,59,166. Learned Authorised Representative referring to the decision of the Hon'ble Supreme Court in Topman Exports v/s CIT, [2012] 342 ITR 49 (SC), submitted, the face value of DEPB credit would be covered by section 28(iiib), hence, entitled to deduction under section 80HHC. He submitted, profit arising on transfer of such credits would be covered by section 28(iiid), hence, the limitation provided in Fourth provision under section 80HHC(3) would only apply to such profits. Learned Authorised Representative submitted, the assessee would be entitled to deduction in respect of face of value of DEPB credit as no disallowance under Fourth proviso to section

80HHC(3) can be made because the DEPB have been transferred at a loss. Learned Authorised Representative submitted, otherwise also, the issue is covered by the decision of the Tribunal in assessee's own case for the assessment year 2001–02.

31. Learned Departmental Representative submitted, the issue may be restored back to the Assessing Officer for deciding in terms of the decision of the Hon'ble Supreme Court in Topman Exports (supra).

32. We have considered the submissions of the parties and perused the material available on record. It is the claim of the assessee that as per section 28(iiid), only the profit on transfer of DEPB credit can be treated as income of the assessee. He submitted, as in the impugned assessment year, the assessee has incurred loss on sale of DEPB. There is no income to the assessee in terms of section 28(iiid) having considered the submissions of the assessee in the light of the relevant statutory provisions and the decision of the Hon'ble Supreme Court in Topman Exports (supra), we find force in the submissions of the assessee. Moreover, it is seen, similar issue arose in assessee's own case for assessment year 2001–02. The Tribunal, while deciding the issue in appeal preferred by the Department held as under:–

> *"After considering the rival submissions and perusing the relevant material on record we find that the issue raised through this grounds is no more res integra in view of the judgment of the Hon'ble Supreme Court in the case of Topman Exports v. ITO [(2012) 67 DTR 185 (SC)] in which it has been held that when DEPB is sold by a person, his profit on transfer of DEPB will be sales value of DEPB less its face value. It has further been held that DEPB is chargeable as income u/s 28(iiib) in the year in which such person applies for DEPB against the exports and profit on sale of DEPB is chargeable under section 28(iiid) in the year in which he transfers DEPB. Respectfully following the precedent we set aside the impugned order on this issue and direct the Assessing Officer to allow the*

claim in accordance with the aforesaid judgment of the Hon'ble Supreme Court."

33. Respectfully following the aforesaid decisions of the Hon'ble Supreme Court and co–ordinate bench of the Tribunal, we restore the matter back to the file of the Assessing Officer to allow assessee's claim in terms of principle laid down by the Hon'ble Supreme Court.

34. In ground no.5, assessee has challenged the addition made on account of transfer pricing adjustment relating to disallowance of interest on the advances made to overseas subsidiaries.

35. Brief facts are, the assessee is engaged in the business of manufacturing of generic pharma and nutritional products. It exports formulations, packing material and bulk drugs to its overseas group of companies hereinafter called A.Es. Though, the assessee had subsidiaries located in U.S.A., Mexico, Switzerland, Brazil, Uruguay, U.A.E. and South Africa, however, subsidiaries located in U.S.A., Brazil and Mexico are engaged in manufacturing activities. Other subsidiaries are engaged in trading activities only. During the relevant previous year, assessee entered into international transactions with its A.E. as under:–

Sr. no.	*International Transaction*	*Amount (₹ in crore)*	*Method Applied*
1.	*Sale of packing material and bulk drug*	*6.37*	*TNMM*
2.	*Export of finished goods*	*58.47*	*Cost Plus*
3.	*Sale of equipment*	*0.46*	*TNMM*
4.	*Reimbursement* *Received – ₹0.60 crore* *Paid ₹2.52 crore*	*3.12*	*Actual*

36. In the course of assessment proceedings, the Assessing Officer noticing that assessee has entered into international transactions with its A.E. made a reference to the Transfer Pricing Officer for determining arm's length price of the transactions. The Transfer Pricing Officer after verifying the transfer pricing study and other relevant facts and material on record, made an adjustment of ₹ 86,10,000, to the price charged for export of manufactured goods. Further, the Transfer Pricing Officer found that the assessee has paid interest amounting to ₹ 29.49 crore on various credit facilities availed by it. He also found that advances to subsidiary companies were of significant value. He noticed that advances are on account of various expenses incurred by the assessee on behalf of the subsidiary companies which have to be recovered by it. The Transfer Pricing Officer was of the view that either the assessee should have recovered the expenditure incurred from subsidiary or it should have charged interest. The Transfer Pricing Officer observed while on the one hand the assessee was incurring interest expenditure on the credit facilities availed, on the other hand, the subsidiary companies are benefiting by availing interest free funds from the assessee. He, therefore, opined that a charge has to be made on account of interest receivable by the assessee from the subsidiary companies on the extended credit facility provided to them. From the information available on record, he found that a sum of ₹ 10.56 crore is outstanding as advances from subsidiary companies. He, therefore, called upon the assessee to work out the interest on such advances outstanding from subsidiaries. As stated by the Transfer Pricing Officer, assessee without prejudice to its claim that no interest is chargeable submitted a note working out the interest on advances made by applying rate of 6.9% per annum which as per the Transfer Pricing Officer is the weighted average rate on the

loan availed by the assessee. Though, while objecting to charge of interest on the outstanding advances to the subsidiary, the assessee contended that subsidiary companies have generated significant sales and the margin generated by them is more than other transactions, however, the Assessing Officer did not accept the contention of the assessee on the reason that the assessee had not brought on record any contemporaneous document to show that interest was not charged having regard to the volume and margins on the A.E. transactions. Secondly, according to the Transfer Pricing Officer, interest chargeable is on account of financial cost which has nothing to do with profit at the operational level. Accordingly, he determined the arm's length price for the interest free credit extended to the assessee at ₹ 13,05,113 and made an adjustment. In terms of the adjustment made by the Transfer Pricing Officer, the Assessing Officer completed the assessment. Though, the assessee challenged the addition made on account of transfer pricing adjustment of the advances made to the subsidiary but the learned Commissioner (Appeals) dismissed the same by observing that the assessee was not able to justify its claim that no interest should be charged on the interest free advances to the subsidiary. Learned Commissioner (Appeals) observed, as the assessee was paying heavy interest on borrowing, whereas it has advanced money free of interest to subsidiary, the TPO was justified in determining the ALP of interest free advances.

37. Learned Authorised Representative submitted, the transfer pricing provision contained under Chapter–VI of the Act, is a computation provisions and not a charging provision. When the assessee has not charged any interest on the advance made to the subsidiary, no income has arisen to the assessee from the

international transaction. Therefore, no transfer pricing adjustment could be made on notional basis. He submitted, advancing of loans to the A.E. cannot be regarded as an international transaction. He submitted, overseas subsidiaries have been formed by the assessee with a view to market its pharmaceutical products in the respective countries and to establish its business in the overseas jurisdiction. He submitted, receivables recorded in the books of account are towards expenditure incurred by the assessee on behalf of its A.Es. He submitted, such expenditures were incurred by the assessee from interest free funds / internal accruals and no borrowed funds were utilised for incurring such expenditure. Therefore, as there was no cost to the assessee in respect of the interest free advances, no charge on account of notional interest on the advance to subsidiary should be made. Learned Authorised Representative submitted, the assessee had not actually advanced any amount in cash to the A.Es. The expenditure incurred by the assessee was inextricably connected with the conduct of assessee's business. Such fact is evident from the significant sales generated by the A.E. in respective of jurisdictions in the succeeding assessment years. Learned Authorised Representative submitted, as the expenditure incurred was for commercial / business expediency, notional interest cannot be computed on the advance made to subsidiaries. Without prejudice to the aforesaid submissions, learned Authorised Representative submitted, in any case of the matter, if the advancement of interest free funds to the subsidiary is treated as international transaction, the interest rate to be applied by using LIBOR instead of INR rate. He submitted, during the relevant year, the prevailing LIBOR was 1.698% which could be considered in case it is held that interest is chargeable on the interest free advance to the subsidiary. Learned Authorised Representative referring to the

working furnished before the first appellate authority, contended that the average cost of borrowing during the relevant assessment year was 4.34%. He, therefore submitted, LIBOR plus 200 basis points can be considered as the rate of interest.

38. Learned Departmental Representative, on the other hand, submitted, as per the amended provisions of section 92B, the expression *"International Transaction"* would include capital financing including receivable or any other due arising during the course of business. Therefore, assessee's claim that interest free advances would not constitute international transaction is not acceptable. Learned Departmental Representative submitted, once the interest free advances are held to be coming within the ambit of international transaction, then determination of arm's length price of such transaction is imperative. He submitted, the interest free advance is in effect extended credit period granted to the A.E. for receivables. Hence, arm's length price has to be determined as per method prescribed under section 92C. He submitted, since the assessee has exported goods to A.Es and non–A.Es and there is delay in realisation of export proceeds from both there is internal CUP available to bench mark its transactions. Therefore, the same needs to be applied to bench mark the international transaction and TNMM is not a preferable method. Learned Departmental Representative submitted, the contention of the assessee that the loan is for business expediency would have no effect as the assessee advanced loan without charging any interest whereas it is bearing interest cost on credit facilities availed. Therefore, the assessee has shifted its profit based to the overseas A.E. who have benefited at the cost of the assessee. He submitted, if the assessee had not advanced such interest free funds

or allowed extended credit facility, then there would not have been any need for the assessee to avail interest bearing credit facility as it could have utilised the surplus funds / internal accruals for its business purposes. He, therefore, submitted that the assessee's claim that no interest on notional basis is chargeable is not acceptable. As far as the rate of interest applicable, the learned Departmental Representative submitted, domestic Prime Lending Rate (PLR) is to be applied.

39. We have considered the submissions of the parties and perused the material available on record. As far as the contention of the learned Authorised Representative that the interest free advances to the overseas subsidiary on account of reimbursement of expenditure is not an international transactions and the transfer pricing provisions are not applicable, we are not convinced with the same. On a reference to section 92B of the Act, it is observed that after amendment effected vide Finance Act, 2012, with retrospective effect from 1st April 2002, the definition of international transactions as provided under the Explanation (i) to section 92B, has been expanded to include the following transactions.

> *"Explanation.—For the removal of doubts, it is hereby clarified that—*
>
> *(i) the expression "international transaction" shall include—*
>
> *(a) the purchase, sale, transfer, lease or use of tangible property including building, transportation vehicle, machinery, equipment, tools, plant, furniture, commodity or any other article, product or thing;*
>
> *(b) the purchase, sale, transfer, lease or use of intangible property, including the transfer of ownership or the provision of use of rights regarding land use, copyrights, patents, trademarks, licences, franchises, customer list, marketing channel, brand, commercial secret, know-how, industrial*

property right, exterior design or practical and new design or any other business or commercial rights of similar nature;

(c) capital financing, including any type of long-term or short-term borrowing, lending or guarantee, purchase or sale of marketable securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business;

(d) provision of services, including provision of market research, market development, marketing management, administration, technical service, repairs, design, consultation, agency, scientific research, legal or accounting service;

(e) a transaction of business restructuring or reorganisation, entered into by an enterprise with an associated enterprise, irrespective of the fact that it has bearing on the profit, income, losses or assets of such enterprises at the time of the transaction or at any future date;"

40. On a plain reading of clause (c) of Explanation–(i) to section 92B, it is evident that any type of advance payment or deferred payment or receivable or any other debt arising during the course of business including capital financing would come within the scope of *"International Transaction"*. Thus, the assessee having incurred expenditure on behalf of its overseas A.Es which are receivables from the A.Es comes within the meaning of *"International Transactions"*. Therefore, contention of the learned Authorised Representative that receivables on account of expenditure incurred on behalf of A.E. are not international transaction or no computation can be made is not acceptable in view of specific statutory provisions. The next contention of the learned Authorised Representative is, the assessee has long standing business relation with the subsidiary and as a result of investment / advances made, assessee has derived benefit as substantial sales have been recorded from the geographical locations where the subsidiaries are situated. In our view, plea of business /

commercial expediency are not applicable to such type of transactions. Under the transfer pricing provisions, it has to be seen whether a particular transaction between the related parties is at arm's length. Therefore, it has to be seen whether under similar circumstances, assessee would have entered into such transaction with unrelated parties. If the facts on record suggest that the assessee would not have entered into such type of transactions with unrelated parties, then the transaction between the related parties cannot be considered to be at arm's length. There is no dispute to the fact that while the assessee has incurred cost by availing credit facility it has advanced interest free funds by not charging interest on the expenditure incurred on behalf of the subsidiaries. Therefore, certainly, a benefit has accrued to the subsidiary on account of the assessee whereas a part of the profit base of the assessee on account of cost incurred on credit facility has been shifted to the subsidiary which otherwise could have been avoided if the surplus funds were available with it. In these circumstances, the principle of commercial expediency would not come into play. Therefore, in our view, as the assessee has not charged interest on outstanding receivables from the overseas subsidiaries, arm's length price of the same has to be determined. Having held so, it is necessary to quantify the rate of interest of such transaction. It is observed, the Transfer Pricing Officer has applied the average interest rate of domestic credit facility availed by the assessee. However, it is seen from the material on record, the entire expenditure incurred by the assessee on behalf of the overseas subsidiary are on foreign currency (dollar), therefore, domestic PLR rate in terms of Indian rupee cannot be applied. It has been brought to our notice through the working submitted before the Departmental Authorities that the average cost of borrowings to the assessee is 4.84%. The learned

Authorised Representative has also submitted a working showing the average LIBOR rate of financial year 2002–03 at 1.698%. In a number of decisions, different benches of the Tribunal have consistently held that in such type of international transaction, domestic PLR rate cannot be applied and the rate of interest has to be quantified either with reference to LIBOR or EURIBOR depending upon the country and currency in which the transaction has taken place. Considering the facts of the present case, we are of the considered opinion that LIBOR rate of 1.698% plus 300 basis point would be the appropriate interest rate applicable to the international transactions relating to advancement of interest free loan / extended credit facility to the overseas A.E. Accordingly, we direct the Assessing Officer / Transfer Pricing Officer to compute the interest on the interest free advances paid to the A.E. Ground no.5, is partly allowed.

41. In the result, assessee's appeal is partly allowed.

ITA no.274/Mum./2007 – Department's Appeal
C.O. no.121/Mum./2007 – Assessee's Cross Objection

42. Ground no.1, in Department's appeal corresponding to ground raised by the assessee in its cross objection relates to disallowance made by the Assessing Officer out of interest expenditure.

43. Brief facts are, during the assessment proceedings, the Assessing Officer notic that in the relevant previous year as per the balance sheet of the assessee, it had made investment in subsidiary companies to the tune of ₹ 125.39 crore, out of which investment in overseas company are of ₹ 113.77 crore and in Indian subsidiary of ₹ 10.21 crore. The Assessing Officer observed, as per the record pertaining to earlier assessment year proportionate interest was disallowed on

account of investment made for establishing subsidiary overseas. On the basis of those facts, Assessing Officer called upon the assessee to explain why in the impugned assessment year also interest proportionate to investment in overseas company should not be disallowed. In response to the query raised to the Assessing Officer, it was submitted by the assessee that 30% of its sales turnover was generated from Central and South American market. Therefore, investment made in overseas subsidiary is inextricably connected with the export business of the assessee. Therefore, the investment is wholly and exclusively for the purpose of business. It was further submitted, investment made in overseas subsidiary having been made out of surplus fund / internal accruals available with the assessee on which no interest payment is made proportionate interest should not be disallowed. The assessee submitted, as far as the long term borrowings are concerned, they have been utilised for investment in fixed asset and long term working capital requirement of the company. Short term borrowings is utilised for day–to–day needs for working capital of the company. It was further submitted, during the year assessee has repaid ₹ 44 crore of interest bearing loans by obtaining FCNR loan from State Bank of India of ₹ 43 crore @ 3.26% interest rate. Thus, it was submitted by the assessee, if at all any disallowance of interest has to be made, the same should be restricted to the interest charged @ 3.26%. Alternatively, assessee also submitted, if the interest is not allowable as business expenditure, the same has to be allowed under section 57(iii). The Assessing Officer, however, did not find merit in the submissions of the assessee. The Assessing Officer, after considering the loan taken and investment made in overseas subsidiary yearwise observed that borrowed funds have been diverted for making investment. Hence, interest on such borrowed

funds is not allowable as business expenditure. Accordingly, the Assessing Officer working out interest cost of 10% on the investment in subsidiary from assessment year 2000–01 to 2003–04 and computed the total disallowance out of interest expenditure at ₹ 8,05,87,632. Being aggrieved of such disallowance, assessee preferred appeal before the learned Commissioner (Appeals).

44. Before the first appellate authority, it was submitted by the assessee by furnishing a fund flow statement that assessee had sufficient interest free funds to invest in overseas subsidiaries. However, learned Commissioner (Appeals) observed that assessee had not disputed the allegation of the Assessing Officer that borrowed funds were not utilised for investment in shares of overseas company.

45. As far as the claim of commercial expediency is concerned, the learned Commissioner (Appeals) observed, assessee has not demonstrated how the investment in subsidiary has helped in furthering the business of the assessee. He, therefore, upheld the disallowance of proportionate interest made by the Assessing Officer. However, he observed that as the income from subsidiary by way of dividend is taxable as income from other sources, the interest expenditure on account of investment in subsidiary would be eligible for deduction under section 57(iii) of the Act. In this regard, he relied upon the order passed by his predecessor–in–office in assessee's own case for the assessment year 2002–03.

46. Learned Departmental Representative though agreed that in assessment year 2002–03, learned Commissioner (Appeals)'s view in allowing deduction of interest expenditure under section 57(iii) was upheld by the Tribunal but he nevertheless submitted, assessee having

not proved the commercial expediency, proportionate disallowance out of interest expenditure is valid. Learned Authorised Representative contesting the claim of the Department and also relying upon the ground raised in cross objection submitted, during the year assessee has sufficient interest free funds available with it by way of surplus and reserve and internal accruals to make the investment and there being no nexus established by the Department that borrowed funds were utilised for investment in shares of overseas companies, proportionate disallowance of interest expenditure cannot be made as presumption would be the investments made were out of interest free funds available with the assessee. Learned Authorised Representative referring to the balance sheet of the company as at 31st March 2003, submitted, while the total investment in overseas company were to the tune of ₹ 114 crore, interest free funds available with the assessee were of ₹ 230.37 crore. He submitted, the incremental investments made during the year are out of internal cash accruals and from the infusion of equity capital and not from debt / borrowed funds.

47. Learned Authorised Representative submitted, assessee has made investment in fixed asset during the year which was out of borrowed funds, therefore, it cannot be said that the borrowed funds were not utilised for the purpose for which they were availed. He submitted, in any case of the matter, as the assessee had mixed funds, both interest bearing and interest free presumption would be investments made in subsidiary were out of interest free funds. For such proposition, he relied upon the decision of the Hon'ble Jurisdictional High Court in CIT v/s Reliance Utilities and Power Ltd. [2009] 331 ITR 340 (Bom.), and HDFC Bank Ltd. v/s DCIT, W.P. no.1753 of 2016. Further, learned Authorised Representative

submitted, there is enough documentary evidence brought on record to show that the overseas subsidiaries are acting as marketing arms of the assessee. He submitted, as a result of investment made by the assessee in establishing the overseas subsidiary, the sales in certain geographical locations has substantially increased. In this context, he drew the attention of the Bench to the transactions with the subsidiary companies. He submitted, from the aforesaid facts, it is clear that the assessee has a regular trade / business transaction with the overseas subsidiary, therefore, there is close business connection between the assessee and the overseas subsidiary. Thus, the commercial expediency having been established, no disallowance can be made in terms of section 36(1)(iii). In this context, he relied upon the decision of Hon'ble Madras High Court in Indian Commerce & Industries Co. (P) Ltd. v/s CIT, [1995] 213 ITR 533 (Mad.). He, therefore, submitted no disallowance out of interest expenditure can be made. As far as the direction of the learned Commissioner (Appeals) for allowing deduction under section 57(iii), learned Authorised Representative submitted, in assessment year 2002–03, assessee had agreed for deduction under section 57(iii) as there was sufficient interest income to set–off the interest expenditure. However, in the impugned assessment year, set–off of interest expenditure against interest income, would result in a loss which the assessee cannot carry forward. He, therefore, submitted that as the reason on which the assessee accepted deduction under section 57(iii) in assessment year 2002–03 is absent in the impugned assessment year, his acceptance of decision of the learned Commissioner (Appeals) in respect of deduction under section 57(iii) in assessment year 22–03, should not operate against him in claiming deduction in the impugned assessment year under section 36(1)(iii). Learned Authorised Representative submitted, the investment made

for acquiring shares of subsidiary companies is also for control over the subsidiary. Hence, interest expenditure is allowable under section 36(1)(iii).

48. We have considered the submissions of the parties and perused the material available on record. It is evident from the orders of the Departmental Authorities, though the assessee had contended that borrowed funds were utilised for acquiring fixed asset and working capital, whereas, interest free funds available through reserve and surplus and internal accruals were utilised for advance to the subsidiary but the Assessing Officer had rejected such claim of the assessee and disallowed proportionate expenditure from the interest cost alleging utilisation of borrowed funds towards investment in shares of foreign subsidiary. It has been brought to our notice by the learned Authorised Representative by furnishing a summary of cash flow that during the financial year 2002–03, the total interest free funds to the assessee by way of internal accruals and infusion of equity was to the tune of ₹ 14,93,70,838, whereas the investment made in subsidiary was to the tune of ₹ 14,30,50,843, thereby stile leaving a surplus interest free funds available with the assessee of ₹ 63,19,996. Moreover, the assessee has contended before the Departmental Authorities and also has stated before us, borrowed funds were utilised for the purpose for which they were availed by investing in fixed assets and working capital. Aforesaid, contentions of the assessee was not considered by the Departmental Authorities with any genuineness. When the Assessing Officer makes the disallowance of interest expenditure on the allegation that borrowed funds were utilised for the purpose of investment in subsidiary, the burden is on

the Assessing Officer to establish the nexus between the borrowed funds and the investments made. Establishment of such nexus assumes more importance when it is found that along with borrowed funds, assessee had sufficient interest free funds available with him to make the investment. In such situation, as held by the Hon'ble Jurisdictional High Court in Reliance Utilities Pvt. Ltd. (supra), subsequently following in HDFC Bank Ltd. (supra), the presumption would be investment in subsidiary has been made out of own surplus funds available with the assessee. In the present case, the fact that assessee has sufficient interest free funds available with it, has not been controverted by the Department. In such circumstances, following the ratio laid down by the Hon'ble Jurisdictional High Court as referred to above no disallowance in terms of section 36(1)(iii) can be made on account of interest attributable to investment / advance made in overseas subsidiary. Another aspect of the issue is whether the advance / investment made is on account of commercial expediency. It is seen from the material placed on record that the assessee had made investment for establishment of the overseas subsidiary to expand its market has in other geographical locations. It is not disputed by the Departmental Authorities that as a result of aspect of overseas subsidiary, there is substantial increase in sales in such geographical location. Therefore, the contention of the assessee that overseas subsidiaries are acting as the marketing arms of the assessee cannot be disputed or denied. Moreover, it is seen from the record that the assessee has regular business transactions with overseas subsidiary by supplying raw material, etc. for manufacture of goods. Further, the assessee has also sold finished goods to the A.Es. All these factors clearly establish that there is a business / trade relationship between the assessee and overseas subsidiary. That being

the case, it cannot be said that investments made are not wholly and exclusively for the purpose of business. Thus, any interest expenditure attributable to such investment / advance to overseas subsidiary would be allowable under section 36(1)(iii) as it is wholly and exclusively for the purpose of business. As held by the Hon'ble Supreme Court in S.A. Builders (supra) and subsequently reiterated in Hero Cycles Ltd. (supra), commercial expediency has to be seen through the position of a prudent businessman and the Assessing Officer cannot step into the shoes of a businessman to find out the necessity or reasonableness of expenditure incurred. Thus, in our view, for the aforestated reason, no disallowance out of interest expenditure can be made. As far as the findings of the learned Commissioner (Appeals) that assessee is eligible for deduction under section 57(iii), we are of the view that only because the assessee accepted the decision of the learned Commissioner (Appeals) in assessment year 2002–03, for whatever may be the reason that will not deprive the assessee from claiming deduction of interest expenditure under section 36(1)(iii). It may be a fact that in assessment year 2002–03, considering that there was enough interest income against which the interest expenditure could be set–off, hence, there is no impact on the tax liability, the assessee might have accepted the decision of the learned Commissioner (Appeals). Moreover, it may be a fact that at relevant point of time, the assessee did not had the benefit of decision of the Hon'ble Jurisdictional High Court which could have led the assessee not to accept the decision of the learned Commissioner (Appeals). Thus, on over all consideration of the facts and circumstances of the case, we allow assessee’s claim by deleting the addition of ₹ 8,05,87,632. Thus, we allow the ground

raised by the assessee in cross objection and dismiss the ground raised by the Department.

49. In ground no.2, Department has challenged allowance of assessee's claim of deduction in respect of employer's contribution made towards PF / ESIC.

2. Before us, both the parties admitted, the issue arising out of the aforesaid ground is identical to ground no.3, raised by the assessee in its appeal in ITA no.641/Mum./2007, wherein, vide Para–21, the said issue is decided in favour of the assessee and against the Revenue. Consistent with the view taken therein, we allow this ground also.

50. In ground no.3, assessee has challenged the decision of the learned Commissioner (Appeals) in respect of rejection of indirect cost by 10% of the export incentives for computing profits under section 80HHC.

51. Brief facts are, during the assessment proceedings, the Assessing Officer, while perusing the note attached to report in form no.10CCAC, noticed that while working out indirect cost of trading export for claiming deduction under section 80HHC, assessee has reduced the indirect cost of trading export by 10% of the export incentives and other income. He, therefore, called upon the assessee to justify the method adopted by the assessee. In response, it was submitted by the assessee that 10% of export incentive was reduced from indirect cost debited to Profit & Loss account as the same was deemed to have been incurred for earning incentive. In this regard, assessee relied upon the Special Bench decision of the Tribunal in Surendra Engineering Corp. V/s ACIT, [2003] 86 ITD 212. The Assessing Officer,

however, did not accept the contention of the assessee on the reasoning that Department has preferred appeal against the Special Bench decision of the Tribunal before the Hon'ble Jurisdictional High Court and accordingly, held that 10% deduction made by the assessee is not acceptable. Assessee challenged the action of the Assessing Officer before the first appellate authority.

52. Learned Commissioner (Appeals), after considering the submissions of the assessee in the light of the decision of the Tribunal Special Bench held that indirect cost has to be reduced by 10% of the export incentive for calculating profit from trading export.

53. We have considered the submissions of the parties and perused the material available on record. It has been brought to our notice by the learned Authorised Representative that issue is squarely covered by the decision of the Tribunal in assessee's own case for assessment year 2002–03, wherein following its earlier order for assessment year 2001–02, the Tribunal has upheld the order of the learned Commissioner (Appeals). Learned Departmental Representative has not controverted the factual position.

54. On a perusal of the order of the co–ordinate bench of the Tribunal for assessment year 2002–03, in assessee's own case, in ITA no.1727/Mum./2006 dated 16th December 2015, it is noticed that while upholding the order of the learned Commissioner (Appeals) in assessee's own case claim of reduction in indirect cost by 10% of the export incentives the Tribunal followed its own order for assessment year 2001–02 in assessee's own case wherein the Tribunal had decided the issue by following the decision of the Hon'ble Supreme

Court in Hero Export v/s CIT, [2007] 295 ITR 454 (SC). The relevant observations of the Bench is as under:–

> *"7.1. It is noted by us that similar issue came up before the Tribunal in A.Y.2001-02, wherein the Tribunal has upheld the claim of the assessee by relying upon the decision of Hon'ble Supreme Court in the case of Hero Exports vs CIT 295 ITR 454, by making following observations:*
>
> > *"16. Ground no.9 is against the direction of the learned CIT(A) to reduce 10% export incentives from the gross indirect cost by considering the same as indirect expenditure incurred in earning such incidence. Having heard the rival submissions it is noted that this ground is also covered in favour of the assessee by the judgment of the Hon'ble Supreme Court in the case of Hero Exports v. CIT [295 ITR 454 (SC)]. In this case it has been held that the principle of attribution is applicable to cases falling u/s 80HHC(3)(b) and therefore, part of indirect cost has to be apportioned to expenses incurred for earning export incentives. 10% of total income has been held as fair estimate in this case. As the view taken by the learned CIT(A) matches with that of the Hon'ble Supreme Court in the aforenoted case, we are of the considered opinion that no interference can be made in the impugned order on this issue."*
>
> *7.2. Thus, respectfully following the judgment of Hon'ble Supreme Court as well as coordinate bench of Tribunal, we allow this ground in favour of the assessee."*

55. There being no material difference in the facts brought to our notice by the learned Departmental Representative, respectfully following the aforesaid decision of the co–ordinate bench of the Tribunal, we uphold the order of the learned Commissioner (Appeals) by dismissing the ground raised by the Department.

56. Ground no.4, is in relation to treatment of foreign exchange fluctuation gain as business income for grant of deduction under section 80HHC.

57. Brief facts are, during the assessment proceedings, the Assessing Officer noticed that while computing deduction under section 80HHC, assessee has included the foreign exchange fluctuation gain of ₹ 17,61,491 in the business income. Assessing Officer, however, was of the view that export realisation is not directly relatable to the export turnover of the year. He observed that income arising out of exchange rate fluctuation has to be treated as income from other sources. Accordingly, he reduced the same from business income while computing deduction under section 80HHC.

58. The learned Commissioner (Appeals), however, allowed assessee's claim by observing that the exchange fluctuation gain derived by the assessee being part of export turnover is eligible for deduction under section 80HHC.

59. We have considered the submissions of the parties and perused the material available on record. There is no dispute to the fact that foreign exchange gain was directly as a result of export made by the assessee. Moreover, it is observed from the order of the learned Commissioner (Appeals) similar relief was also granted to the assessee in the preceding assessment year. In view of the above, we do not find any infirmity in the order of the learned Commissioner (Appeals). Ground no.4, is dismissed.

60. In ground no.5, the Department has challenged the decision of the learned Commissioner (Appeals) with regard to netting of interest

expenditure against interest income for computation of deduction under section 80HHC.

61. In the course of assessment proceedings, the Assessing Officer noticing that the assessee had included interest earned on fixed deposit in the banks amounting to ₹ 89,82,566, in the business income for claiming deduction under section 80HHC, disallowed the claim by holding that such income being in the nature of income referred to any Explanation (baa) to section 80HHC(4B), 90% of such income has to be reduced from profit of business for computing deduction under section 80HHC.

62. In the appeal preferred by the assessee against the aforesaid decision of the Assessing Officer, learned Commissioner (Appeals) held that the interest received should be netted off against interest payment. He further held that if the interest is generated out of the margin money for issuing guarantee or opening of L/C the same is directly connected with the business of assessee. Hence, the interest income generated from such activities has to be assessed as business income. He, therefore, directed the Assessing Officer to net off interest received and paid and thereafter apply Explanation (baa) to section 80HHC to interest remaining after netting–off.

63. We have considered the submissions of the parties and perused the material available on record. At the outset, learned Authorised Representative submitted, the issue is squarely covered by the decision of the Tribunal in assessee's own case for assessment year 2001–02. Learned Departmental Representative has not controverted the aforesaid factual position. On a perusal of the order dated 16th December 2015, in ITA no.1727/Mum./2006, for assessment year

2002–03, it is noticed that while dealing with identical issue, the Tribunal followed its earlier decision in assessee's own case for assessment year 2001–02, wherein the Tribunal has allowed assessee's claim on the basis of ratio laid down by the Hon'ble Supreme Court in ACG Associate Capsules P. Ltd. v/s CIT, [2012] 343 ITR 89 (SC), the relevant observation of the Bench is as under:–

> *"15.2. We have gone through the order of earlier year and submissions made before us. This issue came up before Tribunal in A.Y. 2001-02 wherein claim of the assessee was allowed by making following observations: "11. Ground no.6 of the Revenue's appeal is against netting of interest receipts for the purpose of deduction u/s 80HHC. The Assessing Officer, while computing deduction u/s 80HHC considered the gross amount of interest. The learned CIT(A), however, overturned this finding by holding that only the net amount of interest was to be considered. Having heard the rival submissions it is noticed that this issue has been settled by the Hon'ble Supreme Court in Associated Capsules Pvt. Ltd. v. CIT [(2012) 343 ITR 89 (SC)] by holding that netting of interest is permissible. The reliance of the ld. DR on the judgment in the case of CIT vs Asian Star Co. Ltd. (2010) 326 ITR 56 (Bom) is misconceived as the same has been reversed by the Hon'ble Supreme Court in the afore-noted case. As such no fault can be found with the impugned order on this score. This ground is not allowed." 15.3. No contrary decision has been brought before us and therefore, respectfully following the order of the Tribunal in earlier year and judgment of Hon'ble Supreme Court, we find no substance in the ground raised by the Revenue and the same is dismissed."*

64. There being no material difference in facts brought to our notice by the learned Departmental Representative, respectfully following the aforesaid decision of the Tribunal, we uphold the order of the learned Commissioner (Appeals) by dismissing ground no.5, raised by the Department.

65. In ground no.6, Department has challenged the decision of the learned Commissioner (Appeals) in directing the Assessing Officer to exclude excise duty and sales tax from the total turnover for computation of deduction under section 80HHC.

66. Brief facts are, while completing the assessment, Assessing Officer held that excise duty has to form part of total turnover for computing deduction under section 80HHC. Though, assessee had excluded the excise duty from the total turnover following the judgment of Hon'ble Jurisdictional High Court in CIT v/s Sudarshan Chemical Industries Ltd. [2000] 245 ITR 769 (Bom.), but the Assessing Officer reasoning that Department has filed SLP against the said decision of the Hon'ble Bombay High Court rejected assessee's contention.

67. The learned Commissioner (Appeals), however, following the decision of the Hon'ble Jurisdictional High Court, as referred to above,, directed the Assessing Officer to exclude sales tax and excise duty from the total turnover for computing deduction under section 80HHC.

68. We have considered the submissions of the parties and perused the material available on record. In the course of hearing, it has been brought to our notice by the learned Authorised Representative that the issue has been decided in favour of the assessee by the Tribunal in assessment year 2001–02 and 2002–03, in assessee's own case following the decision of the Hon'ble Supreme Court in CIT v/s Lakshmi Machine Works, [2007] 290 ITR 667 (SC). On a perusal of the order passed by the Tribunal in assessee's own case for the assessment year 2002–03, it is observed that the Tribunal while deciding the issue held as under:–

"16.1. It has been brought to our notice that this issue is covered by the order of the Tribunal of assessment year 2001-02, wherein relying upon the Supreme Court decision in CIT vs. Laxmi Machine Works 290 ITR 667, it has been held that excise duty should be excluded from the total turnover for the purposes of section 80HHC. Relevant observations of the Tribunal's order are reproduced below:

> *"12. Ground no.7 of the Revenue's appeal is against the direction of the learned CIT(A) to exclude the amount of excise duty on Rs.8.92 crore from `total turnover' for the purposes of computing deduction u/s 80HHC. The Assessing Officer included the amount of excise duty in `total turnover' while computing deduction u/s 80HHC. The learned CIT(A) overturned the assessment order on this point.*
>
> *13. After considering the rival submissions and perusing the relevant material on record we find that this issue has also been settled by the Hon'ble Supreme Court in the case of CIT v. Laxmi Machine Works [(2007) 290 ITR 667 (SC)] holding that the excise duty is not includible in the `total turnover' in the formula contained in section 80HHC. The impugned order on this issue, being in conformity with the view taken by the Hon'ble Supreme Court, does not warrant any interference. This ground is not allowed."*

16.2. No contrary judgment has been placed before us, and therefore, respectfully following judgment of Tribunal and that of Hon'ble Supreme Court, we decide this issue in favour of the assessee and therefore Ground no. 7 of the Revenue's appeal is dismissed."

69. There being no material difference in facts, respectfully following the decision of the co–ordinate bench of the Tribunal, we uphold the order of the learned Commissioner (Appeals) by dismissing the ground raised by the Department.

70. Ground no.7, raised by the Department relates to transfer pricing adjustment in respect of sale of finished goods.

71. Brief facts are, assessee is engaged in the business of generic, pharma and nutritional products. It exports formulation, packing material and bulk drugs to its group companies. As noted by the Transfer Pricing Officer, assessee has subsidiaries located in U.S.A., Mexico, Switzerland and Brazil, Uruguay, U.A.E. and South Africa. He also noted that the subsidiaries located in U.S.A., Brazil and Mexico are engaged in the manufacturing activities, whereas, other subsidiaries are engaged in trading activities. In the course of proceeding before him, the Transfer Pricing Officer after perusing the transfer pricing documents of the assessee and other relevant material found that margin shown by the assessee is much more than the margin of the comparable companies, however, the Transfer Pricing Officer called upon the assessee to show the margin earned in respect of different therapeutic segment with each of the A.Es and the third party margin in the same segment. After considering the information submitted by the assessee, Transfer Pricing Officer noticed that margin earned on transaction with A.E. are lower than the margin earned on the transaction with third parties in respect of two therapeutic segments. Accordingly, he proceeded to determining the arm's length price of two segments by applying the margin earned by the assessee on its third party transactions. By following the aforesaid process, the Assessing Officer made an adjustment of ₹ 86,10,000. In terms of the adjustment made by the Transfer Pricing Officer, the Assessing Officer passed the draft assessment order by making addition of ₹ 86,10,000. Assessee challenged the addition before the learned Commissioner (Appeals).

72. The learned Commissioner (Appeals), after considering the submissions of the assessee vis–a–vis the facts and material on record, found that the method adopted by the Transfer Pricing Officer is not correct in view of various discrepancies / short comings as the Transfer Pricing Officer has not taken into consideration various facets of the transactions. The learned Commissioner (Appeals) held that the Transfer Pricing Officer has made comparison of sale price which were different in terms of packing and marketing. He observed, as far as U.S. market is concerned, the same is more mature and competitive as against smaller market at Cellopharm and Brazil, which forms Latin market part. He further observed, while the sales made to Brazil and Cellopharm are in small packing, which could be termed as ready to use pack not requiring any further processing whereas the bulk sales made to A.E. are not same. He further noticed that in the preceding assessment year, under identical facts and circumstances, the learned Commissioner (Appeals) had held that there was no transfer of profit from assessee to A.E. Thus, on the basis of aforesaid consideration, learned Commissioner (Appeals) held that price charged by the assessee to its A.E. is reasonable requiring no further adjustment.

73. We have considered the submissions of the parties and perused the material available on record. It is observed against the order of the learned Commissioner (Appeals) for assessment year 2002–03, the Department came in appeal before the Tribunal. The Tribunal restored the issue back to the Assessing Officer / Transfer Pricing Officer for fresh consideration observing as under:–

> *"17.6. We have gone through the submissions made by both the sides as well as orders of the lower authorities. It is noted by us that Ld. CIT-DR is factually correct in submitting that CIT(A) has deleted the addition without following the correct*

approach. The issues with regard to transfer pricing adjustment have to be resolved following a mechanism and complying with the provisions as contained in chaper X, dealing with the transfer pricing issues as contained in sections 92-92F and connected rules as contained in Rules 10A,10B,10C,10D and 10E of Income Tax Rules 1962. These sections and rules prescribe various methods that may be employed to establish arm's length price, explaining applicability of each method, the documentation required to be maintained and form of the certificate to be issued by auditors in this regard. These regulations provide that any income arising from the international transactions shall be determined having regard to the arm's length price. This issue has now been decided in various courts that where international transactions are involved with AE, then arm's length price has to be determined in line with the aforesaid provisions. It is noted by us that Ld. CIT(A) has decided this issue without taking into account the effect of these provisions. Therefore, in our considered view, this issue needs to be sent back. On the other hand, the assessee has also made a grievance that the TPO has not made proper analyses while bench marking the transactions to compute arm's length price. It has been further suggested that TNMM method will be most appropriate method. No objection has been raised by the Ld. CIT-DR, in this regard. Therefore, keeping in view all the facts and circumstances of this case, we deem it appropriate to send this issue back to the file of the TPO who shall carry out afresh search and make fresh analysis and shall also keep in view the aforesaid objections raised by the assessee. The TPO shall also give adequate opportunity of hearing to the assessee to submit required details and documents, as per law, before deciding this issue afresh. Thus, with these directions, this issue is sent back to the file of AO/TPO. Thus ground no. 8 of Revenue's appeal is allowed for statistical purposes."

74. On a careful reading of the observations of the co–ordinate bench, it is noticed that they have disapproved the approach / method adopted by the Transfer Pricing Officer while determining the arm's length price as well as the conclusion drawn by the learned Commissioner (Appeals). Therefore, taking into consideration of relevant facts restored the matter back to the Transfer Pricing Officer with direction to make fresh research and fresh analysis keeping in

view the objections raised by the assessee. In the impugned year facts are identical. Therefore, keeping in view of the observations of the Tribunal as referred to above, we restore the matter back to the file of the Assessing Officer with a direction to make a fresh analysis relating to most appropriate method which could be adopted for bench marking the international transaction and, thereafter, undertake a comparably analysis. It is further directed, the Transfer Pricing Officer should consider the objections / submissions of the assessee with regard to adoption of most appropriate method as well as the selection of comparables, etc. Only after considering the submissions of the assessee and affording due opportunity of being heard, the Transfer Pricing Officer shall pass a speaking and reasoned order meeting all the objections raised by the assessee. With the aforesaid direction, the issue is restored to the file of the Assessing Officer. Ground no.7, is allowed for statistical purposes.

75. In ground no.8, the Department has challenged the decision of the learned Commissioner (Appeals) in directing the Assessing Officer not to reduce the deduction computed under section 80HHC, while computing book profit under section 115JB.

76. Brief facts are, while computing the book profit under section 115JB, Assessing Officer reduced the deduction computed under section 80HHC, amounting to ₹ 2,78,66,066, being aggrieved of such computation, assessee challenged it before the learned Commissioner (Appeals).

77. In the course of proceedings before the first appellate authority, it was submitted by the assessee that in the preceding assessment year, the issue has been decided in favour of the assessee. Learned

Commissioner (Appeals), following the decision of his predecessor–in–office, held that export profits deductible in calculating book profit have to be worked out by considering the profit as per the books of account and not the amount allowed as a deduction to the assessee under section 80HHC. Being aggrieved, the Department is in appeal before us.

78. We have considered the submissions of the parties and perused the material available on record. At the outset, learned Authorised Representative submitted before us that the issue has been decided in favour of the assessee by the Tribunal in assessee's own case for the assessment year 2001–02. Learned Departmental Representative also agreed that the Tribunal has decided the issue in favour of the assessee. On a perusal of the order dated 3rd August 2012, in ITA no.6487/Mum./2004, for assessment year 2001–02, it is noticed, the co–ordinate bench following the decision of Hon'ble Supreme Court in Ajanta Pharma Ltd. v/s CIT, [2010] 327 ITR 305 (SC), held as under:–

> *"17. Last ground of the Revenue's appeal is against the direction of the learned CIT(A) to reduce export profits based on book profit in the ratio of export turnover to total turnover and not the quantum of deduction as worked out u/s 80HHC for the purposes of working out `book profit' liable for MAT u/s 115JB of the Act.*
>
> *18. After considering the rival submissions and perusing the relevant material on record we find that this issue is directly covered in favour of the assessee by the judgment of the Hon'ble Supreme Court in the case of Ajanta Pharma Ltd. v. CIT [(2010) 327 ITR 305 (SC)] in which it has been held that clause (iv) of the Explanation to section 115JB covers full export profits of 100% as `eligible profits' and the same cannot be reduced to 80% by relying on section 80HHC(1B). Thus it is evident that the learned CIT(A) has taken an inescapable view on this point which does not require any interference. This ground is not allowed."*

79. There being no material difference in facts, respectfully following the aforesaid decision of the co–ordinate bench, we uphold the order of the learned Commissioner (Appeals) by dismissing the ground raised by the Department.

80. In the result, Department's appeal is partly allowed for statistical purposes and assessee's cross objection is allowed.

ITA no.4063/Mum./2010 – Department's Appeal

81. Ground no.1 relates to acceptance by the learned Commissioner (Appeals) assessee's claim of deduction under section 80HHC in respect of sales effected to Mission Pharma Logistic Pvt. Ltd.

82. Brief facts are, the Assessing Officer in the course of assessment proceedings, while verifying assessee's claim of deduction under section 80HHC, noticed that during the relevant previous year, assessee had effected sales to another entity viz. Mission Pharma Logistic Pvt. Ltd. and claimed deduction under section 80HHC, on such sales. Assessing Officer observed that Mission Pharma Logistic Pvt. Ltd. is not doing any manufacturing activity and is only engaged in re–packing liberalising, kit packing, etc. He, therefore, opined that Mission Pharma Logistic Pvt. Ltd. is not eligible for deduction under section 10A. Referring to sub–section (4C) of section 80HHC, the Assessing Officer called upon the assessee to explain why deduction under section 80HHC on sales made to Mission Pharma Logistic Pvt. Ltd. should not be disallowed. Though, assessee objected to proposed disallowance by stating that the concerned company being a SEZ unit, sales effected to such unit will be considered as deemed export and, hence, eligible for deduction under section 80HHC, however, the Assessing Officer on the basis of his conclusion that Mission Pharma

Logistic Pvt. Ltd. is not eligible unit under section 10A, disallowed assessee's claim under section 80HHC on such turnover. Being aggrieved of such disallowance, assessee challenged the same in appeal before the learned Commissioner (Appeals).

83. Learned Commissioner (Appeals), after considering the submissions of the assessee held that as the assessee has fulfilled the condition of 80HHC(4C), it is eligible for deduction. While coming to such conclusion, learned Commissioner (Appeals) observed the entity to which the assessee has effected sales is an unrelated party and the Assessing Officer has not brought any material on record to substantiate his conclusion. The learned Departmental Representative relying upon the observations of the Assessing Officer, submitted that in terms of section 80HHC(4C), assessee has to fulfill two conditions; firstly, the unit to which sales is effected must be situated in SEZ and secondly, such SEZ unit should be eligible for deduction u/s 10A.

84. Learned Departmental Representative submitted, though, the assessee fulfilled first condition but the second condition was not fulfilled as the assessee failed to establish the fact that Mission Pharma Logistic Pvt. Ltd. is eligible for deduction under section 10A.

85. Learned Authorised Representative strongly supporting the reasoning of the first appellate authority submitted, the Assessing Officer while disallowing assessee's claim of deduction 80HHC, has failed to substantiate his allegation with supporting evidence that Mission Pharma Logistic Pvt. Ltd. is not engaged in manufacturing activity. He, therefore, submitted, no adverse inference can be drawn with reference to the conclusion of the learned Commissioner (Appeals).

86. We have considered the submissions of the parties and perused the material available on record. Undisputedly, assessee has set–up a unit outside SEZ for manufacturing and sale of generic pharma products and other nutritional products. It is also not disputed that assessee during the relevant previous year, has sold its products worth ₹ 3,33,62,706 to Mission Pharma Logistic Pvt. Ltd. a company set–up in SEZ and claimed deduction under section 80HHC, on such sales turnover. On a perusal of sub–section (4C) of section 80HHC, it is noticed that an assessee having set–up a unit outside SEZ engaged in manufacture / production of goods or merchandise, if sells such products to any undertaking situated in SEZ which is eligible for deduction under section 10A, then such sales effected by the assessee shall be deemed to be export out of India for the purpose of section 80HHC. Thus, on a plain reading of the provisions contained in sub–section (4C) of section 80HHC, it becomes clear that to qualify as deemed export out of India three conditions are to be satisfied. Firstly, assessee claiming such deduction must have set–up an undertaking for manufacture or production of goods outside SEZ; secondly, the goods / products manufactured by it, should be sold to an undertaking situated in SEZ; thirdly, such SEZ units must be eligible for deduction under section 10A. In the present case, there is no dispute between the parties that assessee has satisfied conditions no.1 and 2. As far as condition no.3, is concerned, it is the allegation of the Assessing Officer that SEZ unit to which assessee has effected sales viz. Mission Pharma Logistic Pvt. Ltd. is not an eligible unit under section 10A, as it is not engaged in any manufacturing activity but is doing only re–packing, re–labeling and kit packing. However, on what basis, the Assessing Officer has come to such conclusion has not been indicated in the assessment order. The learned Commissioner (Appeals), while

allowing assessee's claim has given a categorical finding that there is no basis for the Assessing Officer to conclude that Mission Pharma Logistic Pvt. Ltd. is not eligible under section 10A. Learned Departmental Representative has not been able to bring to our notice the material / evidence on the basis of which the Assessing Officer has concluded that the SEZ unit to which assessee has effected sales is not eligible under section 10A. Therefore, conclusion drawn by the Assessing Officer being merely on conjecture and surmises without substantiated by positive evidence cannot be accepted. More so, when he does not dispute the fact that Mission Pharma Logistic Pvt. Ltd. is an SEZ unit. In the aforesaid facts and circumstances, department has failed to establish / demonstrate with cogent material that Mission Pharma Logistic Pvt. Ltd. is not eligible for deduction under section 10A, we are not able to interfere with the findings of the learned Commissioner (Appeals). Accordingly, upholding the order of the learned Commissioner (Appeals) on this issue, we dismiss ground no.1, raised by the Department.

87. In ground no.2, Department has challenged the decision of the learned Commissioner (Appeals) in accepting assessee's claim of deduction under section 80HHC in respect of profit derived on transfer of DEPB credit.

88. This issue is similar to the issue raised in ground no.4, of assessee's appeal in ITA no.641/Mum./2007, dealt by us in the earlier part of the order. Following our reasoning given in Para–30, we uphold the order of the learned Commissioner (Appeals) by dismissing the ground no.2, raised by the Department.

89. In ground no.3, Department has challenged the decision of the learned Commissioner (Appeals) in rejecting indirect cost by 10% of the export incentives for computing profit from trading exports under section 80HHC.

90. Similar issue arose in Department's appeal in ITA no.274/Mum./ 2007, dealt by us in ground no.5. Following the reasoning given in Para–50 to 52, we uphold the order of the learned Commissioner (Appeals) by dismissing the ground no.3, raised by the Department.

91. In ground no.4, Department has challenged the decision of first appellate authority for netting of interest receipts against interest payment for computation of deduction under section 80HHC.

92. This issue is similar to the issue raised in Ground no.5, by the Department in its appeal in ITA no.274/Mum./2007. Following the reasoning given in Para–60 and 61, we uphold the order of the learned Commissioner (Appeals) by dismissing the ground no.4, raised by the Department.

93. In ground no.5, Department has challenged the decision of the learned Commissioner (Appeals) in deleting the adjustment made to the arm's length price by the Assessing Officer and the Transfer Pricing Officer.

94. This issue is similar to the issue raised in ground no.7, by the Department in its appeal in ITA no.274/Mum./2007. Following the reasoning given in Para–70 and 71, we uphold the order of the learned Commissioner (Appeals) by dismissing the ground no.5, raised by the Department.

95. In the result, Department's appeal is dismissed.

C.O. no.61/Mum./2011
(Assessee's Cross Objection arising out of Department's appeal in ITA no.4063/Mum./2010)

96. Ground no.1, relates to disallowance of deduction claimed under section 35(2AB) of the Act.

97. This issue is similar to the issue raised in Ground no.1, by the assessee in its appeal in ITA no.641/Mum./2007. Following the reasoning given in Para–8 and 9, we set aside the impugned order passed by the learned Commissioner (Appeals) and allow the ground no.1, raised by the assessee.

98. Ground no.2, relates to transfer pricing adjustment of ₹ 22,19,174, in respect of outstanding receivables / debit balance of foreign subsidiary.

99. This issue is similar to issue raised in ground no.2, by the assessee in its appeal in ITA no.641/Mum./2007, wherein vide Para–16 and 17, we have partly allowed the claim of the assessee. Consistent with the findings given therein, we direct the Assessing Officer to re–compute / charge interest in terms of our finding as aforesaid. Ground no.2, is also partly allowed.

100. In ground no.3, assessee has challenged the computation of book profit under section 115JB of the Act, after reducing the deduction under section 80HHC.

101. This issue is also similar to the issue raised by the Department in ground no.8, in its appeal in ITA no.274/Mum./2007, wherein we have

dismissed the ground raised by the Department. The only difference is, the learned Commissioner (Appeals) has decided the issue against the assessee. However, there being no material difference in facts between the impugned assessment year and in assessment year 2003–04, consistent with the findings given in Para–75 and 76, we set aside the impugned order passed by the learned Commissioner (Appeals) on this issue and allow the ground no.3, raised by the assessee.

102. In the result, assessee's cross objection is partly allowed.

103. To sum up, assessee's appeal in ITA no.641/Mum./2007 is partly allowed, Department's appeal in ITA no.274/Mum./2007 is partly allowed for statistical purposes, assessee's cross objection no.121/ Mum./2007 is allowed, Department appeal in ITA no.4063/Mum./2010 is dismissed and assessee's cross objection no.61/Mum./2011 is partly allowed.

Order pronounced in the open Court on 29.04.2016

Sd/-	**Sd/-**
ASHWANI TANEJA	**SAKTIJIT DEY**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

MUMBAI, DATED: 29.04.2016

Copy of the order forwarded to:
(1) The Assessee;
(2) The Revenue;
(3) The CIT(A);
(4) The CIT, Mumbai City concerned;
(5) The DR, ITAT, Mumbai;
(6) Guard file.

True Copy
By Order

Pradeep J. Chowdhury
Sr. Private Secretary

(Dy./Asstt. Registrar)
ITAT, Mumbai