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THE HIGH COURT OF DELHI AT NEW DELHI

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Judgment reserved on: 08.09.2011
Judgment delivered on: 04.11.2011

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ITA Nos. 1110/2006 & 1111/2006

COMMISSIONER OF INCOME TAX

..... APPELLANT

Vs

M/S ASAHI INDIA SAFETY GLASS LTD.

..... RESPONDENT

Advocates who appeared in this case:

For the Appellant: Mr Sanjeev Rajpal, Advocate
For the Respondent: Mr M.S. Syali, Sr. Advocate with Mr O.P. Sapra, Ms Mahua Kalra & Ms Husnal Syali, Advocates.

CORAM :-

**HON'BLE MR JUSTICE SANJAY KISHAN KAUL
HON'BLE MR JUSTICE RAJIV SHAKDHER**

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| 1. | Whether the Reporters of local papers may be allowed to see the judgment ? | Yes |
| 2. | To be referred to Reporters or not ? | Yes |
| 3. | Whether the judgment should be reported in the Digest ? | Yes |

RAJIV SHAKDHER, J

1. The captioned appeals pertain to assessment years 1997-98 and 1998-99. The Income Tax Appellate Tribunal (hereinafter referred to as the 'Tribunal') had by a common judgment dated 29.12.2005 disposed of three appeals pertaining to the aforementioned assessment years. Out of the three appeals, two appeals had been filed by the revenue, while the third appeal had been filed by the assessee. The revenue had filed appeals for both the assessment years, i.e., 1997-98 and 1998-99, while the



assessee had filed an appeal only qua assessment year 1997-98. However, before us the common ground is that the appeals pertained to a singular issue, though the amounts involved differ in each of the captioned assessment years. Therefore, we have framed the following questions of law for assessment years 1996-97 and 1998-99, which, as would be evident, apart from the amounts involved are otherwise identical:

Assessment year 1998-99

Whether ITAT was correct in law in holding that the expenditure of Rs 1,70,68,811/- incurred by the assessee on account of software and professional expenses was a revenue expenditure?

Assessment year 1997-98

Whether ITAT was correct in law in holding that the expenditure of Rs 1,36,77,664/- incurred by the assessee on account of software and professional expenses was a revenue expenditure?

2. Given aforesaid circumstances, following facts are required to be noticed in order to adjudicate upon the issues culled out above:

2.1 The assessee it appears had installed a software in the financial year 1996-97, relevant for assessment year 1997-98. The software was installed by Arthur Anderson & Associates, which is an accounting and consulting firm, pursuant to an agreement dated 25.06.1996 executed with the assessee. The software was based on application software, commonly known as, oracle application. In respect of this, an agreement appears to have been executed between the assessee and Oracle Software India Pvt. Ltd. The agreement between the assessee and Arthur Anderson & Associates



inter alia adverted to the manner in which oracle application had be implemented.

3. In the assessment year 1997-98, the assessee had amortized an expenditure amounting to Rs 1,36,77,664/- towards software and professional expenses under the head “deferred revenue expenditure”. It is pertinent to note that the assessee had not written off any part of this expenditure in its books of accounts, during the assessment year 1997-98; though, while computing its taxable income the assessee claimed the entire amount as expenditure on revenue account. In the succeeding assessment year, i.e., 1998-99, an additional expenditure in the sum of Rs 1.71 crores was claimed as deduction. During the assessment proceedings conducted in respect of assessment year 1997-98, the assessing officer noticed the aforementioned aspect and, therefore, called upon the assessee to give details of the nature of software purchased and, the period by which it was likely to be replaced. The assessee responded to the query raised, by broadly stating as follows:

“a) that software technology is very rapidly changing and hence there is no enduring benefit.

b) In the instant case, software has been installed for carrying on the assessee’s business more efficiently and that the said expenditure has not brought into existence any asset which is capable of being source of income.

c) that the software installed in F.Y. 96-97, due to various deficiencies, had to be upgraded in the following F.Y. and



an additional expenditure of Rs 1.71 crores was incurred for this purpose.”

3.1 The Assessing Officer, however, did not accept the explanation given by the assessee, and thus, proceeded to disallow the deduction claimed by the assessee. Briefly, the reasons for doing so were as follows:

- (i) the expense was incurred by the assessee towards an ‘intensive project’ with the idea of overhauling the method accountancy, and to efficiently train the accounting staff of the assessee;
- (ii) the project spanned over a period of 18-24 months;
- (iii) the expenditure incurred by the assessee had accorded long term benefit to it – since it would serve the assessee’s purpose for a number of years as also the fact that it would enhance the income of the assessee;

3.2 The fact that the assessee had incurred an expenditure in the succeeding year as well weighed with the Assessing Officer in coming to the conclusion that the expenditure incurred had brought about enduring benefit to the assessee.

3.3 Towards this end, the Assessing Officer also observed that the expenditure incurred in the financial year 1997-98 (assessment year 1998-99) was towards a “project” and not for ‘upgradation of an existing project or for rectification of mistakes’.

3.4 The Assessing Officer, broadly for the foregoing reasons, as indicated above, rejected the claim for deduction and, as a matter of fact also denied, it appears, the depreciation allowance to the



assessee on the ground that there was no clarity as to whether the relevant period the assessee had put the software to use.

3.5 In the assessment year 1998-99 the Assessing Officer followed the rationale adopted by his predecessors in the earlier assessment year, i.e., 1997-98 and for the reasons given therein (i.e., that the expenditure was incurred towards an ongoing project) disallowed the deduction claimed, by treating the expenditure incurred, in the sum of Rs 1,70,68,811/-, as capital expenditure. It appears that for the very same reason that there was no material to show that the software had been used in the relevant period, i.e., assessment years 1998-99, depreciation was also disallowed to the assessee. However, the assessee was allowed deduction under Section 80IA, after taking into account the aforementioned disallowance.

4. Being aggrieved, the assessee preferred appeals with the Commissioner of Income Tax (Appeals) [hereinafter referred to as 'CIT(A)'] in respect of orders passed by the Assessing Officer for both the assessment years, i.e., 1997-98 and 1998-99. The CIT(A), in respect of both appeals passed a common order. After noticing at great length the terms of the agreement entered into between the assessee and Arthur Anderson & Associates, the submissions of the parties and, the judgments cited on the issue; he came to the conclusion that the assessee's claim for both the assessment years, i.e., 1997-98 and 1998-99 had to be allowed.

5. The revenue being aggrieved by the decision of the CIT(A) preferred an appeal to the Tribunal. The Tribunal, as indicated



above, passed a common judgment after noticing the aforementioned facts in respect of the said assessment years. The Tribunal returned the following finding of facts.

(i) The assessee was in the business of manufacturing of automobile safety glass; broadly of two types, tempered and laminated, and that its main source of income was from the said activity.

(ii) During the financial year 1996-97 (assessment year 1997-98) the assessee had embarked upon a major computerization programme in the area of financial accounting, purchases, inventory, production, planning and control.

(iii) Arthur Anderson & Associates presented a software package produced by Oracle Corporation, USA, distributed through its associates Oracle Software India Pvt. Ltd., vide its offer letter dated 25.06.1996. The said letter set out the contours of what the software application envisaged. The software application broadly dealt with financial accounting, inventory and purchase. The assessee in terms of the arrangement arrived at with Arthur Anderson & Associates was required to pay professional fee to it, and that on the assessee accepting the offer of Arthur Anderson & Associates was required to enter into an agreement dated 28.06.1996 with Oracle Software India Pvt. Ltd. The said agreement was titled as "Master Software Licence and Service Agreement".



(iv) The software supplied to the assessee was not used as a part of any production process. The agreement with Oracle was a licence agreement which enabled the assessee to use the software.

(v) The assessee did not acquire any ownership in the software application; all rights, title and interest in the application remained in Oracle.

(vi) In return for a right to use the software application, the assessee paid licence fee and 'not any purchase price'.

(vii) In addition to the above, the agreement with Oracle was also provided for extension of maintenance services, for which, the assessee was required to pay an additional fee over and above, the licence fee.

(viii) The licence was terminable under the provisions of the agreement.

(ix) The assessee did not acquire any tangible asset or an asset which created a new source of income or augmented the existing source of income.

(x) The expenses incurred facilitated, management and the conduct of the assessee's business and, thus was not in the nature of a capital expenditure, and

(xi) Lastly, the expenditure incurred by the assessee allowed it to run its business '**more efficiently**' and perhaps '**more profitably**'.

5.1 The expenditure incurred in the aforementioned assessment years was found as having been broadly incurred under following sub-heads:



- (a) Licence fee;
- (b) Annual technical support fee;
- (c) Professional charges;
- (d) Data entry operator charges;
- (e) Training charges; and
- (f) Travelling expenses.

5.2 Therefore, none of these expenses, according to the Tribunal resulted in creation of new asset or a new source of income. The expenses incurred were as per the Tribunal recurring in nature, expended either to upgrade the system or run the system.

6. Being aggrieved by the aforementioned judgment of the Tribunal, the revenue preferred an appeal to this court.

6.1 On behalf of the revenue arguments were advanced by Mr Sanjiv Rajpal, while on behalf of the assessee submissions were made by Mr M.S. Syali, learned senior counsel. The learned counsel for the revenue in support of his arguments relied upon the orders passed by the assessing officer in the two assessment years to demonstrate that the expenditure incurred was of a capital nature as it would enure to the benefit of the assessee for a long period of time.

6.2 Mr Rajpal submitted that the very fact that a huge expense had been incurred in the financial year 1997-98 (assessment year 1998-99) would show that the expenditure was not incurred for the purposes of upgradation or for correction of deficiencies, as has been found by the Tribunal.



6.3 The learned counsel, thus, contended that the deduction claimed by the assessee ought to be disallowed and the view taken by the Tribunal and the CIT(A) on the said issue, consequently, be reversed.

6.4 In support of his submissions Mr Rajpal also highlighted the fact that the assessee in its books of accounts had not debited the expenditure and, as a matter of fact, had attempted to amortize the expenditure over a number of years. This, according to Mr Rajpal, was a clear indicator that the expenditure as per the assessee's own understanding was not made on revenue account.

7. On the other hand Mr Syali appearing for the assessee contended that it is well settled in a catena of judgments, both of this court and of the Supreme Court, that merely because an expenditure results in an enduring benefit would not be a sufficient reason to treat the expenditure incurred as one expended on capital account. Mr Syali submitted that what had to be deciphered in the facts and circumstances of each case, the real intent and purpose of the expenditure, to ascertain as to whether it resulted in bringing into existence a capital asset. In support of his submissions learned counsel relied upon the following judgments:

CIT vs Indian Visit.com (P) Ltd. (2009) 176 Taxman 164 (Del); CIT vs GE Capital Services Ltd. (2008) 300 ITR 420(Del); CIT vs K & Co. (2003) 181 CTR (Del) 378; CIT vs Sumitomo Corporation India, ITA No. 48/2005 dated 28.07.2005; Khem Singh Sankhla vs



UOI & Ors. (2003) 181 CTR 380 (Raj); CIT vs Varinder Agro Chemicals Ltd. (2009) 309 ITR 272 (P&H); CIT vs Southern Roadways Ltd. (2008) 304 ITR 84 (Mad); CIT vs Arawali Constructions Co. (P) Ltd. (2003) 259 ITR 30 (Raj.); CIT vs Raychem RPG Ltd. in ITA No. 4176/2009 dated 04.07.2011 of Bombay High Court; CIT vs Southern Roadways Ltd. (2007) 288 ITR 15 (Mad); Chief CIT vs O.K. Play India Ltd. passed in ITA No. 414/2006 dated 25.02.2011 by the Punjab & Haryana High Court; CIT vs Sundaram Clayton Ltd. (2010) 321 ITR 69 (Mad) and CIT vs Voith Paper Fabrics India Ltd passed in ITA No. 777/2010 dated 07.02.2011 by the Punjab & Haryana High Court.

8. Having heard the learned counsel for the parties, what has emerged on facts as found by the authorities below is as follows: The assessee is in the business of manufacturing safety glass which is used in automobiles. Thus the main source of income of the assessee is from the said activity. The assessee appears to have entered into an agreement with Arthur Anderson & Associates in the financial year 1996-97 (assessment year 1997-98) for installation of a software application for assistance in areas related to financial accounting, inventory and purchase. It has emerged that an offer was made in respect of such a software application by Arthur Anderson & Associates, which find a reflection in a letter dated 25.06.1996. The said agreement between the assessee and Arthur



Anderson & Associates also required the assessee to enter into back-to-back agreement with Oracle. The reasons perhaps being that the software application supplied by the Author Anderson & Associates worked on oracle application. It is precisely for this reason that Arthur Anderson & Associates required the assessee to enter into a licence agreement with oracle titled Master Software Licence and Services Agreement. The assessee was thus, required to pay : apart from the fee to Arthur Anderson & Associates qua its agreement with it; licence fee to Oracle. As a matter of fact Oracle also offered support and maintenance services for which a further additional fee was required to be paid to Oracle.

8.1 The assessee thus admittedly in respect of the aforesaid transactions incurred an expenditure to the tune of Rs 1,36,77,664/- and Rs 1,70,68,811/- in assessment years 1997-98 and 1998-99 respectively. In the books of accounts for the assessment years 1997-98 the assessee had not written off any sum, while in the succeeding assessment year, i.e., 1998-99 the assessee had written off a part of the expenditure amounting to Rs 9,91,228/-.

8.2 Given these facts, could it be said that the expenditure incurred by the assessee in the aforementioned assessment years was in the nature of capital expenditure.

9. The revenue in support of its stand has taken recourse to the test of enduring benefit. It is in our view now somewhat trite to say that the test of enduring benefit is not a certain or a conclusive test which the courts can apply almost by rote. What is required to be



seen is the real intent and purpose of the expenditure and whether the expenditure results in creation of fixed capital for the assessee. It is important to bear in mind that what is required to be seen is not whether the advantage obtained lasts forever but whether the expense incurred does away with a recurring expense(s) defrayed towards running a business as against an expense undertaken for the benefit of the business as a whole. In other words, the expenditure which is incurred, which enables the profit making structure to work more efficiently leaving the source of the profit making structure untouched, would in our view be an expense in the nature of revenue expenditure. Fine tuning business operations to enable the management to run its business effectively, efficiently and profitably; leaving the fixed assets untouched would be an expenditure in the nature of revenue expenditure even though the advantage may last for an indefinite period. Test of enduring benefit or advantage would thus collapse in such like cases. It would in our view be only truer in cases which deal with technology and software application, which do not in any manner supplant the source of income or added to the fixed capital of the assessee. [See ***Alembic Chemical Works Co. Ltd. vs CIT (1989) 177 ITR 377***; ***CIT vs J.K. Synthetics (2009) 309 ITR 371 at page 412*** and ***CIT Vs. Indian Visit.com (supra)***].

9.1. This is the approach which the Supreme Court has applied even in cases where there is a once for all or a lump sum payment. What is to be seen in the facts of this case, as already noticed by us



hereinabove, that the assessing officer as a matter of fact h returned a finding that the expenditure undertaken was for overhauling the accountancy of the assessee and to efficiently train the accounting staff of the assessee. The Tribunal, which is decidedly the final fact finding authority has after noticing the material on record observed that the expenditure was incurred under various sub-heads, which included licence fee, annual technical support fee, professional charges, data entry operator charges, training charges and travelling expenses. The final figure was a consolidation of expenses incurred under these sub-heads. The Tribunal, in our view, and rightly so, came to the conclusion that none of these resulted in either creation of a new asset or brought forth a new source of income for the assessee. The Tribunal classified the said expenses as being recurring in nature to upgrade and/or to run the system.

10. In the background of the aforementioned findings, it cannot be said that the expenses brought about in an enduring benefit to the assessee. The assessing officer was perhaps swayed by the fact that in the succeeding financial year, i.e., 1997-98 (assessment year 1998-99), the amount spent was large. First of all, the extent of the expenditure cannot be a decisive factor in determining its nature. As observed by the Tribunal, the assessee in the relevant assessment year had a turnover of Rs 150 crores and that even without this expenditure it would have continued to achieve the said turnover; though the expenditure incurred in issue would have



enabled it to run its business more efficiently. Therefore, the rationale supplied by the assessing officer in support of its order which found resonance in submissions of the learned counsel for the revenue is, in our view flawed and, hence it would have to be rejected.

10.1. Secondly, the mere fact that the assessing officer records that the expenditure, in financial year 1997-98 (assessment year 1998-99), was incurred towards what he terms as an 'on-going project' would not ipso facto give it a colour of capital expenditure. A careful reading of the Tribunal's judgment show that after noticing the submission of the assessee that the expenditure incurred in the said assessment year was for removing deficiencies which were found in the software installed in the earlier assessment year, and that, out of a sum of Rs 1.71 crores a sum of Rs 49 lacs was incurred to modify, customize and upgrade the software installed, while the balance expenditure was used for development and implementation – it returned a finding that the expenses were incurred to upgrade and run the system. In view of these findings we are of the opinion that assessing officer discovered an erroneous principle on the basis of which he denied the exemption to the assessee.

11. Software is nothing but another word for computer programmes, i.e., instructions, that make the hardware work. Software is broadly of two types, i.e., the systems software, which is also known as the operating system which controls the working of the computer; while the other being applications such as word



processing programs, spread sheets and data base which perform the tasks for which people use computers. Besides these there are two other categories of software, these being: network software and language software. The network software enables groups of computers to communicate with each other, while language software provides with tools required to write programmes. (See Microsoft Computer Dictionary, 5th Edition "Software" at page 489).

12. The aforesaid would show that what the assessee acquired through Arthur Anderson and Associates was an application software which, enabled it to execute tasks in the field of accounting, purchases and inventory maintenance. The fact that the application software would have to be updated from time to time based on the requirements of the assessee in the context of the advancement of its business and/or its diversification, if any; the changes brought about due to statutory amendments by law or by professional bodies like the Institute of Chartered Accountants of India, which are given the responsibility of conceiving and formulating the accounting standards from time to time, and perhaps also, by reason of the fact that expenses may have to be incurred on account of corruption of the software due to unintended or intended ingress into the system – ought not give a colour to the expenditure incurred as one expended on capital account. Given the fact that there are myriad factors which may call for expenses to be incurred in the field of software applications, it cannot be said that either the extent of the expense or the expense being incurred



in close proximity, in the subsequent years, would be conclusive determinative of its nature. The assessing officer has, in our view, erred precisely for these very reasons.

13. Before we conclude, we may also deal with the one last issue raised by the learned counsel for the revenue which is that in the books of accounts, the assessee had not written off the expense in issue, while in the succeeding assessment year only a part of the expense had been written off and, therefore, the assessee's own understanding of the nature of the expense involved was that it was expended on capital account.

13.1 The aforesaid submission is only to be stated to be rejected. The reason being: that the treatment of a particular expense or, a provision in the books of accounts can never be conclusively determinative of the nature of the expense. An assessee cannot be denied a claim for deduction which is otherwise tenable in law on the ground that the assessee had treated it differently in its books. The observation of the Supreme court in the case of Kedar Nath Jute Manufacturing Co. Ltd. vs CIT (1971) 82 ITR 363 puts this beyond doubt. The relevant observations of the Supreme court on this aspect of the matter are extracted hereinbelow: *".....Whether the assessee is entitled to a particular deduction or not will depend on the provision of law relating thereto and not on the view which the assessee might take of his rights nor can the existence or absence of entries in the books of accounts be decisive or conclusive in the matter".....*



13.2 Therefore, the aforesaid contention is of no avail to the assessee's revenue.

14. For the foregoing reasons, we are of the view that the questions of law for each of the aforementioned assessment years have to be answered in the affirmative and in favour of the assessee. Resultantly, the aforementioned appeals are dismissed.

RAJIV SHAKDHER, J

SANJAY KISHAN KAUL, J

NOVEMBER 04, 2011
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