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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

\+ ITA 885/2016, C.M. APPL.45914/2016

PR. COMMISSIONER OF INCOME TAX (CENTRAL) - 3
..... Appellant

Through : Sh. Zoheb Hossain, Sr. Standing Counsel with Sh. Deepak Anand, Jr. Standing Counsel.

versus

SEAGRAM MANUFACTURING PRIVATE LTD.(NOW PEMOD RICHARD INDIA PVT. LTD.) ..... Respondent

Through : Sh. Amit Shrivastava, for Sh. Deepak Chopra, Advocate.

CORAM:
HON'BLE MR. JUSTICE S. RAVINDRA BHAT
HON'BLE MR. JUSTICE NAJMI WAZIRI

O R D E R

% 09.12.2016

1. The revenue is aggrieved by an order of the Income Tax Appellate Tribunal (ITAT) dated 12.04.2016. It urges three questions of law [hereafter referred by their question numbers]:

> *"1. Whether on the facts and in circumstances of the case, Ld. ITAT was correct in sustaining the deduction claimed by the assessee against the gain in repayment of foreign loans due to fluctuations in Foreign Exchange Rate?*
>
> *2. Whether in a situation, where the advertisement and promotion expenses incurred by the assessee over its products also increases the brand popularity of its parent company, a part of such expenditure pertaining to the brand building of the parent company can be allowed to the assessee?*

3. Whether the advertisement and promotion expenditure incurred by the assessee have an enduring benefit to the assessee as it creates tangible asset being goodwill, reputation and credibility and if yes, whether it can be treated as capital expenditure?"

2. So far as Question No.3 - Advertising and Promotion Expenditure is concerned, the issue has been concluded in an identical case in the matter of another group company, in *Principal CIT v. M/s. Seagram Distilleries Pvt. Ltd.* [ITA 224-225/2016, decided on 06.04.2016]. Question No.3, therefore, does not arise for consideration.

3. So far as Question No.1 is concerned, learned counsel relies upon another decision of the Supreme Court in – *Assistant Commissioner of Income Tax v. Elecon Engineering* 2010 (4) SCC 482, to emphasize that if the borrowing is for a particular purpose, the gain has to follow that purpose and, therefore, should be treated as falling in the revenue or capital stream, as the case may be, having regard to such purpose. It is submitted that the said decision in *Elecon (supra)* was rendered after the judgment in *CIT v. Woodward Governor India Private Limited* 2009 (13) SCC 1.

4. In the present case, the assessee had claimed loss on account of foreign exchange fluctuation. The assessee had availed of external commercial loans from its parent company - Seagram Netherlands Antilles NV, the repayment of which was to commence six years from the date the loan was availed/drawn. The Assessing Officer (AO), therefore, held that the liability fell into the capital stream. The CIT(A) followed the decision in *Woodward (supra)* and held in the

assessee's favour. The ITAT confirmed that decision.This Court notices that *Elecon (supra)* undoubtedly is a later decision. The Court emphasised the purpose of the loan and stated that if it was for the financing of fixed asset or working capital, for the ascertainment of it, all relevant circumstances and materials ought to be gone into. The assessee in that case had not produced any worthwhile material. In the circumstances, the Supreme Court held that the revenue's contentions were correct.

5. This Court is of the opinion that the decision in *Woodward (supra)* was correctly applied. Section 43A of the Income Tax Act, 1961 which applies in such circumstances, *inter alia* requires the treatment of foreign exchange fluctuation to follow the purpose of the borrowing; yet it also highlights that, *"the amount by which the liability aforesaid is so increased or reduced during the previous year shall be added to, or, as the case may be, deducted from, the actual cost of the asset."* This Court notices that there is no finding by the AO that the cost of the asset had been reduced or increased, as the case may be, on account of foreign exchange fluctuation. In the circumstances, the findings rendered are not only factual but, in our opinion, in conformity with the previous rule in *Woodward (supra).* The question of law sought to be urged by the revenue is answered against it.

6. Regarding Question No.2, during the course of proceedings in the relevant Assessment Year 2003-04, the AO disallowed 10% from the expenditure on brand enhancement on the ground that it was allocable to the overseas owner/collaborator. The AO reasoned that

any enhancement in the brand presence of the assessee invariably had a fall-out *vis-a-vis* brand value of the overseas IPR proprietor. The AO also recorded the relevant facts that not all brands which belong to the overseas owner were available in the Indian market and in the eventuality of the brand proprietor deciding to wind-up operations, its reputation would still remain intact. The CIT(A), however disagreed with this reasoning. The ITAT confirmed the order but with little or seconded or no reasoning.

7. The expenses in this case were incurred by the assessee. The arrangement *inter alia* between the assessee and the brand proprietor was such that specified required brands were made available in the assessee deals. No doubt, the profits reported were put through the recourse of transfer pricing exercise for the purpose of Arm's Length Price determination. Yet, the fact remains that the overseas owner did not set up any other licensee, at least in the area where the assessee operated, to operate as a rival. Under the Trade Mark Act, especially Section 48, as long as the arrangement existed, the assessee, who was a licensee of the products, was entitled to claim them as business expenditure though in the ultimate analysis they might have enhanced the brand of the overseas owner. No doubt, if the arrangements were terminated, the brand presence of the overseas owner of the articles/IPR would have subsisted. But that would nevertheless subsist in any event on the theory of trans-national reputation of the IPR owner. In the circumstances, disallowing a certain proportion on an entirely artificial and notional basis from the expense otherwise deductible, in our opinion, was not justified. The question of law is

answered against the revenue. For the above reasons, the appeal fails. It is accordingly dismissed.

S. RAVINDRA BHAT, J

NAJMI WAZIRI, J

DECEMBER 09, 2016
‘ajk’