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* IN THE HIGH COURT OF DELHI AT NEW DELHI
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+ ITA No. 283 of 2017

SUMITOMO CORPORATION ...Appellant
Through: Mr. C.S. Aggarwal, Senior Advocate with Mr. Prakash Kumar, Advocate.

versus

COMMISSIONER OF INCOME TAX ...Respondent
Through: Mr. Sanjay Kumar, Junior standing Counsel.

CORAM:
JUSTICE S.MURALIDHAR
JUSTICE PRATHIBA M. SINGH

<u>O R D E R</u>
% **25.08.2017**

1.This is an appeal by the Assessee under Section 260A (1) of the Income Tax Act, 1961 ('Act') against an order dated 30th November 2016 passed by the Income Tax Appellate Tribunal ('ITAT') in ITA No. 2661/Del/2003 for the Assessment Year ('AY') 1998-99.

2. While admitting this appeal, by the order dated 8th May 2017, this Court framed the following questions of law for consideration:

> "(i) Whether the ITAT was justified in remanding the matter to the Assessing Officer ('AO') for verification of the tax already paid by M/s. G.E. International, US for the amount received from the Assessee despite a categorical finding by the Commissioner of Income Tax (Appeals) ['CIT(A)'] that while considering the allowability of the claim of deduction of Rs. 9.10 crores on which there was no obligation by the Assessee

> applicable as per the provisions of Article 26 (3) of the India Japan Double Taxation Avoidance Agreement (DTAA)?
>
> (ii) Whether the ITAT was justified in reversing the order of the CIT (A) as regards disallowance of Rs. 49,53,244 made by the AO in respect of expenditure of Rs. 99,06,488 on commission paid to the subsidiary for services rendered?"

3. As far as Question (i) above is concerned, by the same order dated 8th May 2017, this Court answered the said question in the negative, i.e. in favour of the Assessee and against the Revenue and set aside the impugned order of the ITAT on that aspect. The appeal was set down for hearing today on Question (ii) above.

4. This Court has heard the submissions of Mr. C.S. Aggarwal, learned Senior counsel appearing for the Assessee, and Mr. Sanjay Kumar, learned Standing counsel for the Revenue.

5. The facts in brief relevant to the issue are that the Appellant-Assessee is a company incorporated in Japan. It is a tax resident of Japan. On 30th November 1998, the Assessee filed its return of income for the AY 1998-99, declaring an income of Rs. 11,69,57,478/-. Subsequently, the Assessee filed its revised return of income on 30th December 1999 whereby the declared income was reduced to Rs. 6,25,46,805/-.

6. The return was picked up for scrutiny. By the assessment order dated 20th February 2000, the AO disallowed Rs. 49,53,244/- out of the claim of Rs. 99,06,488/- being the expenditure incurred on account of commission

paid to Sumitomo Corporation India Private Limited ('SCIPL'). Before the AO, the Assessee furnished details of the services provided by the SCIPL which was incorporated in January, 1997 and became operational in April, 1997. Copies of two service contracts entered into by the Assessee with SCIPL were produced. One was dated 1st April 1997 and contemplated payment of commission at 1.3% of the work done. The commission was payable after completion of the services specified therein. The second contract was of the same date. It specified that commission will be payable at 0.9% for the 'local procurement contract' from 1st April 1997 onwards. This was payable pro-rata after each invoice. The AO, however, took the view that since the Assessee had already entered into agreements with the local sub contractors, in relation to the execution of the Andhra Pradesh Gas Power Corporation Ltd. ('APGPCL Project') "there was apparently no business necessity for intermediately [*sic* 'intermediating'] at the later stage of this project." It was held that the Assessee had failed to prove that "payment to the group entity was wholly and exclusively for the purpose of assessee's business." The AO further noted that a portion of income has been passed on to a group concern which was not liable to pay any tax during the year. Considering the said facts, "a portion of claim is not considered wholly and exclusively for the purposes of business." Accordingly, 50% of the claimed deduction in the sum of Rs. 49,53,244/- was disallowed and added to the income of the Assessee.

7. In the Statement of Facts ('SOF') filed before the Commissioner of Income Tax (Appeals) ['CIT (A)'], the Assessee pointed out that the services provided by SCIPL included intermediating between

(i) Consultants/Engineers of the APGPCL Project

(ii) local lawyers and accountants in India and the Assessee

(iii) General Electric and the Assessee

(iv) sub-contractors and the Assessee.

8. The services provided by SCIPL included following up on the collection of payments from APGPCL. On the above SOF, a remand report was called from the AO by the CIT (A). However, the AO defended the disallowance stating that the method followed by the Assessee *prima facie* appeared to have been "employed for evasion of tax."

9. The CIT (A), by order dated 27th January 2003, allowed the Assessee's appeal. The CIT (A) noted that the payments made to SCIPL were in line with the agreements and were for the business requirement of the Assessee. It was noted that the wisdom of any payment by a company cannot be challenged by the AO and cannot form the basis of *ad hoc* disallowance of the expense claimed by the company, unless evidence was brought on record to show that the expenses were "either only a book entry and actual payments were not made, or that there was a collusive arrangement with the intention of evading tax." On facts, the CIT (A) noted that "Except for doubting this to be so, no case has been made out by the AO to establish his suspicion." Consequently, the disallowance of Rs. 49,53,244/- made by the AO was ordered to be deleted.

10. The Revenue then went in appeal before the ITAT. Relevant to the above issue, the only ground raised was that no part of the commission of

Rs. 49,53,244/- paid by the Assessee to SCIPL was allowable as deduction. The Assessee pointed out that the AO disallowed the expenditure wholly on conjectures and surmises.

11. In the impugned order, the ITAT noted as under:

> “80. We have perused the contentions raised in the light of the records placed before us. It is observed that the assessing officer has disallowed a portion of the expenditure paid by the Assessee to the Sumitomo Corporation India Private Limited by way of commission. The agreement relied upon by the Ld. CIT (A) has been entered into between the Assessee and another company, for purposes of recruitment. It is further it is observed that in most of the projects the Assessee has been directly in touch with the companies and there is no mention of involvement by Sumitomo Corporation India private limited. All agreements entered into by Assessee with various companies for implementation of projects are direct without there being any role played by Sumitomo Corporation India Private Limited. We are therefore in agreement with the disallowance made by the assessing officer and uphold the same.”

12. The Court finds that the ITAT has not bothered to discuss the actual facts of the case relevant to the issues at hand. The observation that all agreements entered into by the Assessee with various companies for implementation of projects were "direct without there being any role played" by SCIPL was factually incorrect and in the teeth of the two contracts entered into by the Assessee with SCIPL, the details of which formed part of the record. It is not at all clear on what basis the AO disallowed 50% of the expenditure. If the AO was of the view that the expenditure incurred was not for the business purposes of the Assessee, he should have disallowed it *in*

toto. However, there had to be some objective basis for deciding that the expenditure incurred was not wholly and exclusively for the purposes of business. As explained by the Supreme Court in ***CIT v. Walchand and Co. P. Ltd. [1967] 65 ITR 381 (SC)***:

> "..In applying the test of commercial expediency for determining whether the expenditure was wholly and exclusively laid out for the purpose of the business, reasonableness of the expenditure has to be adjudged from the point of view of the businessman and not of the revenue."

13. In the present case, both the AO and the ITAT appeared to have proceeded only on surmises and conjectures while holding that 50% of the commission paid by the Assessee to SCIPL should be disallowed. Again, in ***CIT v. Hero Cycles (P) Ltd. [2015] 379 ITR 347 (SC)***, it was cautioned 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 of the board of directors and assume the role to decide how much is reasonably expenditure having regard to the circumstances of the case."

14. In the present case, the payment of commission by the Assessee to SCIPL pursuant to the contract was never in doubt. There was no basis on which the AO could have simply decided that the said expenditure was unnecessary or unreasonable. Merely because the two contracts were of the same date did not mean that they were not wholly and exclusively for the purposes of the business of the Assessee. While the commission under one contract was payable only upon rendering of the services in their entirety,

the commission in the other, which was at a different rate, was for local purchases and payable as and when an invoice was raised. It was not for the Revenue to decide whether such expense was in fact necessary.

15. Accordingly Question (ii) is answered in the negative i.e. in favour of the Assessee and against the Revenue by holding that the ITAT was not justified in reversing the order of the CIT (A) as regards the disallowance of Rs. 49,53,244/- made by the AO in respect of the commission paid to SCIPL for the services rendered. Resultantly, the order of the CIT(A) on this issue is restored, allowing deduction of the entire expenditure of Rs. 99,06,488/- on account of the commission paid by the Assessee to SCIPL.

16. The appeal is accordingly allowed in above terms but, in the circumstances, with no orders as to costs.

S. MURALIDHAR, J.

PRATHIBA M. SINGH, J.

AUGUST 25, 2017
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