IN THE HIGH COURT OF JUDICATURE AT BOMBAY
ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO. 634 OF 2018
WITH
INCOME TAX APPEAL NO. 640 OF 2018

Pr. Commissioner of Income Tax-5,
5th Floor, Room No. 559,
M.K. Road, Mumbai 400 020.]
]
]
].. Appellant

VERSUS

Trigent Software Limited,
201, Vastushilp Annex, 11th Flloor,
Above HDFC Bank,
Gamadia Colony Road, Tardeo,
Mumbai 400 007.].. Respondent
PAN : AABCT2852P

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Mr.Suresh Kumar, Advocate for appellant.

Mr.Chaitanya KK, Senior Advocate with Mr.Prabhakar K. Shetty, Advocate for respondent.

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CORAM : DHIRAJ SINGH THAKUR AND
ABHAY AHUJA, JJ.

Pronounced on : 2nd DECEMBER 2022

: J U D G M E N T :

PER DHIRAJ SINGH THAKUR, J :

1. The present appeals under section 260A of Income Tax Act,

1961 ('the Act') are preferred against the order dated 6th June 2017 passed by the Income Tax Appellate Tribunal, "G" Bench, Mumbai in ITA Nos. 3629/Mum./2015 & 7668/Mum./13 for the assessment years 2006-07 and 2007-08, respectively.

2. In both appeals, the following question of law has been framed, for our consideration :

> *"Whether on the facts and circumstances of the case and in law, the ITAT was right in allowing the capital expenditure in connection with the development of new products as revenue expenditure?"*

3. Income Tax Appeal No. 634 of 2018 :

The assessee is engaged in the business of software development solution and management. The assessee filed its return of income on 31st October 2007 declaring total income at Rs.3,31,29,870/-. The Assessing Officer ('AO') completed the original assessment on a total income of Rs.3,78,61,610/-. Later on, the case was reopened and assessment completed under section 143(3) read with section 147 of the Act. The AO found that the assessee had debited to the profit and loss account an amount of Rs.7.09 crores under the head "Exceptional Items", which expenditure, the AO held after investigation, was incurred

in connection with the development of a new product. The assessee had treated the expenditure as a part of capital work in progress for the assessment years 2004-05 to 2007-08. The development of this software was abandoned and the assessee then claimed the whole capital work in process as revenue expenditure. The AO accordingly made an addition of Rs.7.09 crores.

4. In Income Tax Appeal No. 640 of 2018 :-

The assessee filed its return of income on 30th October 2006 declaring total income at Rs.13,15,321/-. The AO completed the original assessment on a total income of Rs.94,97,912/-. Later on, the case was reopened and assessment completed under section 143(3) read with section 147 of the Act. The AO found that the assessee had debited to the profit and loss account an amount of Rs.81,82,591/- under the head "Exceptional Items", which expenditure, the AO held after investigation, was incurred in connection with the development of a new product. The assessee had treated the expenditure as a part of capital work in progress for the assessment year 2004-05 to 2007-08. The development of this software was abandoned and the assessee then claimed the

whole capital work in process as revenue expenditure. The AO accordingly made an addition of Rs.81,82,591/-.

5. Appeals came to be preferred by the assessee before the Commissioner of Income Tax (Appeals) against the orders of assessment dated 19th March 2013 and 31st December 2013, respectively. The appeals were allowed by the Commissioner of Income Tax (Appeals) partly by holding that the expenditure for the development of a new product by the assessee was in the assessee's existing line of business, and therefore, relying upon the decisions of Delhi High Court in the case of ***Indo Rama Synthetic (I) Ltd. Vs. Vs. Commissioner of Income-tax*** [1] and of Mumbai ITAT in the case of ***IL & FS Education & Technology Services Pvt. Ltd. Vs. ITO***[2]**,** the CIT (A) held that though the assessee had also shown the expenditure as capital work in progress for the assessment years 2004-05 to 2007-08, the deduction had to be allowed as a revenue expenditure in the year in which the project in question was abandoned.

6. The revenue preferred an appeal against the order of the CIT

1 [2011] 333 ITR 18 (Delhi)
2 ITA No.765, Mumbai (2009) dt. 10-04-2013.

(A), dated 31st March 2015 which too, came to be dismissed, by placing reliance upon the judgment of Delhi High Court in the case of ***Indo Rama Synthetic (I) Ltd.*** (Supra) and ***IL & FS Education & Technology Services Pvt. Ltd.*** (Supra). The ITAT upheld the views expressed by the CIT (A), by virtue of its order dated 6th June 2017 impugned in the present appeals.

7. Learned counsel for the appellant urged that the view expressed by the ITAT was unsustainable inasmuch as the expenditure could not have been allowed as revenue expenditure as the assessee had treated the said expenditure as capital in nature and had entered the same in its books of accounts as "Capital work in progress". That expenditure was incurred in connection with the development of a new product, notwithstanding that the new product had not come into existence on account of its viability, expenditure could not have been claimed as revenue expenditure.

8. Learned counsel for the respondent, on the other hand, placed reliance upon the judgment of the Apex Court in ***Empire Jute Co. Ltd. vs Commissioner Of Income Tax*** [3], and ***CIT Vs. EID***

3 1980 124 ITR 1 (SC)

Perry India Ltd. [4] and ***Indo Rama Synthetic (I) Ltd.*** (Supra).

9. Heard learned counsel for the parties.

10. The issue as to whether a particular expenditure incurred was of capital or revenue in nature has been the subject matter of legal debate before various Courts in the Country. As held by the Apex Court in the case of ***Empire Jute Co. Ltd.*** (Supra), since there does not exist an all-embracing formula which can provide a ready solution to the problem; no touchstone has been devised and that every case has to be decided on its own facts keeping in mind the broad picture of the whole operation in respect of which the expenditure has been incurred.

However, it referred to one celebrated test laid down in the case of ***British Insulated & Helsby Cables Ltd. Vs. Atherton*** [5]**.** The principle as stated therein was as under :

> *"When an expenditure is made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital."*

4 257 ITR 253
5 10TC 155

11. However, notwithstanding that a reference had been made to the said principle of law, the Apex Court held that the "enduring benefit test" was not a certain or conclusive test and cannot be applied mechanically without regard to the particular facts and circumstances of a given case and that what was material to consider was the nature of the advantage and that it is only where the advantage was in the capital field that the expenditure would be disallowable on an application of this test. If the advantage consisted merely in facilitating the assessee's trading operations or enabling the management and conduct of the assesse's business to be carried on more efficiently or more profitably, while leaving the fixed capital untouched, the expenditure would be on revenue account, even though the advantage may endure for an indefinite future. The Apex Court held :

> *11 When dealing with cases of this kind where the question is whether expenditure incurred by an assessee is capital or revenue expenditure, it is necessary to bear in mind what Dixon, J. said in Hallstrom's Property Limited v. Federal Commissioner of Taxation 72 CLR 634*
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> > *"What is an outgoing of capital and what is an outgoing on account of revenue depends on what the expenditure is calculated to effect from a practical and business point of view rather than upon the justice classification of the legal rights, if any, secured, employed or exhausted in the process."*

> *The question must be viewed in the larger context of business necessity or expediency. If the outgoing expenditure. is so related to the carrying on or the conduct of the business that it may be regarded as an integral part of the profit-earning process and not for acquisition of an asset or a right of a permanent character, the possession of which is a condition of the carrying on of the business, the expenditure may be regarded as revenue expenditure. See Bombay Steam Navigation Co. (1953) Pvt. Ltd. v. Commissioner of Income-tax(2) The same test was formulated' by Lord Clyde in Robert Addze & Son's Collieries Ltd. v. Inland Revenue(3) in these words:*
>
> > *"Is it part of the company's working expenses, is it expenditure laid out as part of the process of profit earning ? or, on the other hand, is it a capital outlay, is it expenditure necessary for the acquisition of property or of rights of permanent character, the possession of which is a condition of carrying on its trade at all ?"*

12. In ***Indo Rama Synthetic (I) Ltd.*** (Supra), it was held that if the expenditure was incurred for starting a new business which was not carried out by the assessee earlier, then such expenditure would be held to be of a capital nature and it would be irrelevant as to whether the project really materialised or not. However, if the expenditure incurred was in respect of the same business, which was already carried on by the assessee, even if it was for the expansion of the business, I.e., to start a new unit and there was unity of control and a common fund, then such an expense was to be treated as business expenditure. It was held that in such a case whether a new business/asset came into existence or not

would become a relevant factor and that if there was no creation of a new asset, then the expenditure incurred would be of revenue nature and that if the new asset came into existence which was of an enduring benefit, then such expenditure would be of a capital nature.

This view was also followed in the case of ***Commissioner of Income-tax, Ranchi Vs. Tata Robins Fraser Ltd.*** [6]**.**

13. Applying the ratio of the aforementioned judgments in the present case, it can be seen that the appellant is admittedly in the business of development of software solution and management, and therefore, it's endeavour to develop a new software was nothing but an endeavour in its existing line of business of developing software solutions. Admittedly, the product which was sought to be developed, never came into existence and the same was abandoned. No new asset came into existence which would be of an enduring benefit to the assessee, and therefore, in these circumstances, the expenditure could only be said to be revenue in nature.

6 [2012] 211 Taxman 257 (Jharkhand)

14. We are of the view that the view already expressed by the ITAT in the order impugned requires no interference. We find no merit in the present appeals, and the same are accordingly dismissed.

[ABHAY AHUJA, J.] **[DHIRAJ SINGH THAKUR, J.]**