IN THE HIGH COURT OF JUDICATURE AT BOMBAY
ORDINARY ORIGINAL CIVIL JURISDICTION
WRIT PETITION NO. 1323 OF 2012

s Re Services India Pvt Ltd.)
Unit 701-702, Peninsula Corporate Park,)
Tower A, Ganpatrao Kadam Marg,)
Lower Parel, Mumbai 400 013) ..Petitioner

Vs.

1. Deputy Commissioner of Income Tax)
Circle 2(3), Room No.555, Aaykar Bhavan,)
M. K. Road, Mumbai 400 020)

2. Additional Commissioner of Income Tax)
Transfer Pricing – II (4), Room No.19)
Ground floor, Scindia House, Ballard Estate)
Mumbai 400 001)

3. The Union of India through the)
Secretary, Department of Revenue,)
Ministry of Finance, North Block,)
New Delhi 110 001) ..Respondents

Mr. Niraj Sheth a/w Mr. Gunjan Kakad i/b Mr. Atul K Jasani for Petitioner.
Mr. Suresh Kumar for Respondents.

CORAM : K.R. SHRIRAM &
RAJESH S. PATIL, JJ
DATED : 13th OCTOBER 2023

ORAL JUDGMENT (PER K. R. SHRIRAM J.) :

1 Rule is issued on 30th July 2014 and respondents were restrained from acting upon the impugned notice dated 29th March 2010.

2 The petitioner is impugning a notice dated 29th March 2010 issued under section 148 of Income Tax Act 1961 (the Act) for A.Y.-2008-2009.

3 Petitioner filed a return of income on 1st October 2008 for A.Y.-2008-2009 and disclosed a total income of Rs.1,95,75,329/-. The return was

accompanied by a computation of income and profit and loss account along with schedule thereto. Schedule 9 of the profit and loss account enumerates various operative and administrative expenses, which, inter alia, include the rent of Rs.1,18,80,722/- and membership and subscription of Rs.1,98,326/-. The return was accepted and an intimation under section 143 (1) of the act dated 10th May 2009 came to be issued.

4 Petitioner, thereafter, received a notice dated 29th March 2010 under Section 148 of the Act, which is impugned in this petition, in which it was stated that there were reasons to believe that petitioner's income chargeable to tax for A.Y.-2008-2009 had escaped assessment within the meaning of Section 147 of the Act. Petitioner was directed file return of income, which petitioner did. Petitioner was provided with reasons to believe why there was escapement of income. The reasons to believe provided related to two items: 1) deducting rent received at Rs.1.04 in profit and loss account and 2) towards entrance and subscription fees to Willington Sports Club (WSC). The first item that is rent of Rs.1.04 crores, the assessing officer by an order dated 10th October 2011 rejecting petitioner's objection, has dropped the same. That would lead us to consider only the second item that is entrance and subscription fees paid to WSC. The relevant portion of the reasons read as under:

> *"The assessee company has paid Rs.1,98,326/- towards Entrance and Subscription fees to WSC. The benefit of the above payment is long term in nature and should have been considered as Capital Expenditure and should not have been claimed as Revenue expenditure in P & L account."*

5 Petitioner filed its objection through its chartered accountant's letter dated 30th June 2010, in which it was explained that expenditure incurred is towards short term membership renewal fees, i.e., entrance fees Rs.12,360/- and annual subscription fees Rs.1,85,077/- for 1 year and it is incurred for the purpose of the business and hence the same is allowable as claimed. It was submitted that as per the provisions of Section 37 (1) of the Act, any expenditure (not being capital or personal in nature) incurred 'wholly and exclusively' for the purpose of the business of the assessee will be allowed as deduction while computing taxable income of the assessee. It was submitted that expenditure having been incurred wholly and exclusively for the business of the company is revenue in nature and it has been rightly claimed as deduction. Various decisions of various High Courts and Tribunals were also submitted.

6 These objections were rejected by the order dated 10th October 2011. The only basis for rejection is because the benefit of the payment to WSC was long term in nature. How it becomes long term in nature when payment is annual payment, is not even discussed. It is also recorded in the order disposing the objections that the assessee did not produce any bill to substantiate the claim that the expenses were on account of entrance and subscription fees to WSC.

7 The question we are asking is, then how did the assessing officer know that it was towards entrance and subscription fees to WSC as recorded in the reasons to believe because Schedule 9 of the profit and loss account

only mentions membership and subscription of Rs.1,98,326/-. It does not even disclose the name of the club. There is nothing in the reasons to indicate how the assessing officer formed an opinion that those expenditures are long term in nature and should be considered as capital expenditure and could not have been claimed as revenue expenditure on the profit and loss account.

8 Mr Suresh Kumar submitted that the said expenditure cannot be termed as revenue expenditure because it has enduring effect and the assessee is to get the benefits of membership for years to come. Mr Suresh Kumar also submitted that it has been incurred to bring into existence an advantage of enduring benefit of the business and it should be therefore appropriately attriibutable to capital and is in the nature of capital expenditure.

9 We are unable to accept the submissions of the revenue because first of all there is no basis on which the assessing officer has formed a reason to believe that amount of Rs. 1,98,326/- was paid towards entrance and subscription fees to WSC. Schedule 9 of the profit and loss account only enumerates membership and subscription of Rs.1,98,326/- and does not disclose anywhere which club it was.

10 Moreover, petitioner has, in its reply to the notice under Section 148 of the Act, given a breakup of the amount being Rs.12,360/- towards entrance fees and Rs.1,85,077/- towards subscription fees for 1 year and it is incurred for the purpose of business. Even if, we accept what has been

stated in the order disposing objection that petitioner did not produce the bill to substantiate its claim, schedule 9 of the profit and loss account itself discloses that membership and subscription is recurring annual expenditure. In the schedule, it is mentioned for the year ended 31st March 2007 the amount was Rs.2,05,639/- and for the year ended 31st March 2006 the amount was Rs.1,98,326/-. It, therefore, shows that it was an annual expenditure and certainly of a recurring nature and has to be allowed as revenue expenditure.

11 In ***CIT (Large Tax Payer Unit), Centre-1, Mumbai Vs. Lubrizol India Ltd.***[1] , a question that came up for consideration was whether the Tribunal was right in holding that expenses incurred in obtaining club membership is revenue in nature as held by the assessing officer and confirmed by CIT(A). The court was pleased to answer the same and held that it is allowable as revenue expenditure. Paragraph 2 of the order in *Lubrizol India Ltd.* (Supra) reads as under:

> *"2. So far as question A is concerned, the dispute relates to payment of entrace fees for club memberships. The case of the revenue is that the entrance fees is of capital nature while the respondent contends that it is revenue and should be allowed as expenses. The Tribunal in the impugned order has followed the decision of this Court in the case of Otis Elavator Co. Ltd. (India) reported in I95 ITR 682) holding that the entrance fees for the membership of a club would be considered as revenue expenditure. The Tribunal observed that though the entrance fee would have an enduring benefit, it cannot be considered to be capital in nature as no asset was created. Mr. Vimal Gupta, senior counsel on behalf of the revenue submits that the decision of this Court in the matter of Otis Elavator Co. Ltd. (India) (supra) would not be applicable as it did not deal with the payment of entrance fees for membership of the club. However, it is not in dispute that various decisions of the Tribunal had followed the decision of this Court in the matter of Otis Elavator Co. Ltd. (India) (supra) and allowed entrace fees of club as revenue expenditure. Further, this*

1. (2013) 37 taxmann.com 294 (Bombay)

> *Court has also in numerous matters applied the decision of Otis Elavator Co. Ltd.(India) (supra) to the cases were entrance fees of club membership was an issue in dispute and held that the same is allowable as as revenue expenditure. In view of the above, we do not entertain the question as formulated."*

12 The Apex Court in ***United Glass Mgf Co. Ltd.***[2] concluded that Club membership fee of the employees is pure business expense and deductions allowable under Section 37 of the Act. The question that came up for consideration before the Apex Court was whether club membership for employees incurred by the assessee is a business expense and is liable to be deducted under Section 37 of the Act. The Apex Court also referred to various High Court rulings which have held that club membership fee of employee is business expenditure. While answering the question, the Apex Court stated as under:

> *"As far as Question No.2 is concerned, we find that a series of judgments have been passed by High Courts holding that club membership fees for employees incurred by the assessee is business expense under Section 37 of the Income Tax Act 1961. We also find that none of the decisions hae been challenged in this court. Even otherwise, we are of the view that it is a pure business expense."*

13 Hon'ble Gujarat High Court in ***Gujarat State Export Corporation Ltd. Vs. Commissioner of Income Tax***[3] held that it would be difficult to accept the contention of the revenue that the entrance fees paid by the assessee for getting the membership of the sports club can be termed as capital expenditure. Paragraphs 9 and 10 of *Gujarat State Export Corporation Ltd.* (Supra) read as under:

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2. (TS-798-SC-2021)
3. (1994) 209 ITR 649 (Guj)

> *9. Applying the aforesaid test, in our view, it is apparent that, by paying the entrance fee for a sports club, the assessee had no intention to acquire any capital asset or take advantage for the enduring benefit of the business. By commonsense standard, it can be stated that it is for running the business or for bettering the conduct of its business. In the case of Alembic Chemical Works Co. Ltd. (supra), the Court further observed that whether a particular outlay is capital or revenue is required to be determined after taking into consideration various aspects and the relevant criterion is the purpose of the outlay and its intended object and effect, considered in a commonsense way having regard to the business realities. Further, with regard to the test of enduring benefit, the Court observed that in a given case, the test of 'enduring benefit' might break down. For this purpose, the Court relied upon the following observations in the case of CIT vs. Associated Cement Companies Ltd. (1980) 172 ITR 257 (SC) :*
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> *"There may be cases where expenditure, even if incurred for obtaining an advantage of enduring benefit, may, nonetheless, be on revenue account and the test of enduring benefit may break down."*
>
> *10. Applying the aforesaid criterion, in our view, it is apparent that the payment of entrance fee for becoming member of the sports club cannot be termed as a capital expenditure. It is in the nature of an advantage in the commercial sense but it is not an advantage in the capital field. Hence, the Tribunal erred in law in rejecting the claim of the assessee that payment of entrance fee to the Sports Club of Gujarat Ltd. is expenditure of revenue nature and holding that the payment conferred upon the assessee a benefit or an advantage of enduring nature and, therefore, it is expenditure of capital nature. Therefore, question No. 2 requires to be answered in the affirmative for the asst. yr. 1974-75 in favour of the assessee and against the Revenue.*

14 Similarly, the Hon'ble Delhi High Court in ***Commissioner of Income Tax Vs. Samtel Color Ltd.***[4] held that admission fees paid to the club towards corporate membership is wholly and exclusively for business purpose and is revenue in nature. Paragraphs 5 to 5.3 of *Samtel Color Ltd.* (Supra) read as under:

> *"5. Having heard the learned counsel for the Revenue as well as the assessee we are of the view that the impugned judgment of the Tribunal deserves to be upheld for the following reasons:-*
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> *5.1 The expenditure incurred towards admission fee, admittedly, was towards corporate membership. As correctly held by the Tribunal, the*

4. (2010) 326 ITR 425

nature of the expenditure was one for the benefit of the assessee. The 'business purpose' basis adopted for eligibility of expenditure under Section 37 of the Act was the correct approach. This is more so in view of the Tribunal's findings that it was the assessee which nominated the employee who would avail the benefit of the corporate membership given to the assessee.

5.2 The other hurdle for qualification of the expenditure under Section 37 of the Act is that expenditure incurred should not be on capital account. The Assessing Officer came to the conclusion that the expenditure was of a capital nature based on a fallacious reasoning that the expenditure was of an enduring nature and hence on a capital account. It is well settled that an expenditure which gives enduring benefit is by itself not conclusive as regards the nature of the expenditure. We may add that even lump sum payment, which was the case in the instant matter, is not decisive as regards the nature of the payment. See observations in Empire Jute Co Ltd vs. CIT; (1980) 124 ITR 1 (SC) as also the judgment of the Division Bench of this Court in CIT vs. J.K.Synthetics; ITR Nos.139/1988 & 202/1989. The true test for qualification of expenditure under Section 37 of the Act is that it should be incurred wholly and exclusively for the purposes of business and the expenditure should not be towards capital account. In the instant case, as discussed above, the admission fee paid towards corporate membership is an expenditure incurred wholly and exclusively for the purposes of business and not towards capital account as it only facilitates smooth and efficient running of a business enterprise and does not add to the profit earning apparatus of a business enterprise.

5.3 To support the Revenue's contention that the impugned expenditure is on capital account the Learned counsel, Ms Prem Lata Bansal has cited the judgment of the Framatone Connector OEN Ltd vs. DCIT; (2006) 157 Taxmann 116. The said judgment is based on the Supreme Court judgment in the case of Punjab State Industrial Development Corporation Ltd vs. CIT; (1997) 225 ITR 792. The judgment of the Supreme Court on which the Kerala High Court has relied heavily dealt with the issue with regard to fee paid to the Registrar of Companies for increase of authorised capital, that is, whether such an expense was in the nature of revenue or capital expenditure. The Supreme Court came to the conclusion that since the fee was paid to the Registrar of Companies for increase in the capital base of the assessee it was in the nature of capital expenditure. According to us the ratio of the afore-mentioned Supreme Court judgment is not applicable to the expenses incurred on an admission fee for corporate membership. We respectfully disagree with the ratio of the judgment of the Kerala High Court. In turn, we respectfully follow the ratio of the judgment of the Division Bench of this Court in CIT vs. Nestle India Ltd; (2008) 296 ITR 682 and that of the Bombay High Court in the case of Otis Elevator Co (India) Ltd vs. CIT; (1992)195 ITR 682."

15 In our view also the expenditure incurred towards entrance fees and

annual membership would be a revenue expenditure because it has been incurred wholly and exclusively for the purposes of business and not towards capital account. Such expenditure only facilitates the smooth and efficient running of the business enterprise and does not add to the profit earning apparatus of the business enterprise. Therefore, Rule issued on 30th July 2014 is made absolute. The impugned notice dated 29th March 2010 is quashed and set aside,

16 Petition disposed with no order as to costs.

(RAJESH S. PATIL, J.) (K.R. SHRIRAM, J.)