

आयकर अपीलीय अधिकरण, विशाखापटणम पीठ, विशाखापटणम
IN THE INCOME TAX APPELLATE TRIBUNAL,
VISAKHAPATNAM BENCH, VISAKHAPATNAM

श्री वी. दुर्गराव, न्यायिक सदस्य एवं
श्री डि.एस. सुन्दर सिंह, लेखा सदस्य के समक्ष
BEFORE SHRI V. DURGA RAO, JUDICIAL MEMBER &
SHRI D.S. SUNDER SINGH, ACCOUNTANT MEMBER

आयकर अपील सं./I.T.A.No.332/Vizag/2016

(निर्धारण वर्ष / Assessment Year: 2007-08)

ACIT, Circle-2(1),
Guntur

M/s. Veera Associates
Guntur

[PAN No.AAFFV1624C]

(अपीलार्थी / Appellant)

(प्रत्यार्थी / Respondent)

C.O. 55/Vizag/2016

(Arising out of I.T.A.No.332/Vizag/2016)

(निर्धारण वर्ष / Assessment Year: 2007-08)

M/s. Veera Associates
Guntur

ACIT, Circle-2(1),
Guntur

(अपीलार्थी / Appellant)

(प्रत्यार्थी / Respondent)

अपीलार्थी की ओर से / Appellant by

: Shri Deba Kumar Sonowal,
DR

प्रत्यार्थी की ओर से / Respondent by

: Shri S. Rama Rao, AR

सुनवाई की तारीख / Date of hearing

: 08.02.2018

घोषणा की तारीख / Date of Pronouncement

: 21.02.2018

आदेश / O R D E R

PER D.S. SUNDER SINGH, Accountant Member:

This appeal filed by the revenue is directed against order of the Commissioner of Income Tax (Appeals), {CIT(A)}, Guntur vide ITA No.93/CIT(A)-1/GNT/2014-15 dated 29.3.2016 for the assessment year 2007-08.

2. Assessee filed return of income declaring total income of ₹ 3,90,370/- on 3.10.2007. The assessment was completed u/s 143(3) of the Income Tax Act, 1961 (hereinafter called as 'the Act') on 31.12.2009 determining the total income at ₹ 6,90,370/-. Subsequently, the case was reopened u/s 147 of the Act by issue of notice u/s 148 of the Act for not considering the disallowance u/s 40a(ia) of IT Act. During the re-assessment proceedings, the A.O. found that the assessee has made the payment of ₹ 4,36,13,708/- towards the conversion expenses but not deducted TDS as required u/s 194C of the Act, hence made the addition of ₹ 4,36,13,708/- u/s 40(a)(ia) of the Act.

3. Aggrieved by the order of the A.O., the assessee went on appeal before the CIT(A) and made threefold argument. Firstly the assessee argued that the assessee had made short deduction of TDS, but not the non deduction hence, the provisions of section 40(a)(ia) of the Act is not attracted. The second proposition made by the assessee before the

CIT(A) was that the expenditure in question was reimbursement of expenses and TDS has no application. Thirdly relied on the decision of special bench in the case of Merylin Shipping and Transports Vs. ACIT, Visakhapatnam and argued that there was no outstanding payment hence no addition under section 40(ia) is applicable. The CIT(A) allowed the appeal of the assessee placing reliance on the decision of Hon'ble ITAT, Visakhapatnam in the case of Merylin Shipping and Transports Vs. ACIT Visakhapatnam as well as holding that there is no necessity to make TDS on reimbursement of expenses. Accordingly, deleted the addition.

4. Aggrieved by the order of the Ld.CIT(A), the revenue is in appeal before this Tribunal.

5. Appearing for the revenue, Ld. A.R. argued that in view of the Hon'ble Supreme Court decision in the case of Palam Gas Service Vs. CIT(2017) 81 Taxmann.com 43 (SC) the decision of special bench in the case of Merilyn Shipping is no more good law. Further the Ld. D.R. argued with regard to the second proposition of reimbursement of expenses, that this issue was not considered by the Ld. A.O. and the assessee has not brought the issue before the A.O. With regard to the third proposition of short deduction of tax at source, the Ld. D.R. argued that there is no short deduction is a non deduction of tax at source. The

assessee had deducted TDS on payment of ₹ 43,71,049/- and failed to deduct TDS on ₹ 4,36,13,708/-. Hence, the issue is not a short deduction of tax at source and it is the assessee's failure to deduct tax at source. The Ld. D.R. further argued that as per profit & loss account, the assessee has debited the conversion charges into two parts i.e. conversion charges & conversion expenses. On conversion charges, the assessee had made the TDS but on conversion expenses, the assessee did not make the TDS. Both conversion charges and conversion expenses were paid to M/s. Aditya Spinners, therefore, it is clearly evident that the assessee failed to deduct the TDS on which the provisions of section 194C of the Act attracts.. Hence, requested to uphold the order of the assessing officer. With regard to the other proposition submitted by the assessee stating that the respondent has admitted the income in its hands, hence, the assessee should not be treated as assessee in default. The Ld. D.R. submitted that the amendment has come into force with prospective effect but not retrospective, hence argued that the amendment to second proviso of section 40(a)(ia) of the Act is not applicable in the assessment year under consideration. Accordingly, the Ld. D.R. argued that the A.O. has rightly disallowed the expenditure u/s 40(a)(ia) of the Act which require to be upheld.

6. On the other hand, the Ld. A.R. argued that the assessee has made the payments to M/s. Aditya Spinners Pvt. Ltd., a company registered under Companies Act as per job conversion agreement dated 1.4.2006. According to the agreement, the assessee would make the payment of job conversion charges to M/s. Aditya Spinners Pvt. Ltd. for converting spin 30s & 100s count of Polyester staple fibre and viscos staple fibre. For this purpose, the assessee would supply the raw material in required quantities and the contractor M/s. Aditya Spinners would undertake the job work as per the agreement. The expenditure in production i.e. power, wages, production, consumables, etc. would be borne by the assessee and argued that as per the agreement the assessee required to make the payment to M/s. Aditya Spinners, contractors on job conversion charges and the job conversion expenses should be borne by the assessee. Therefore, the Ld. A.R. argued that the job conversion charges would not attract TDS. The job conversion expenses are the reimbursement of expenses and the reimbursement of expenses does not involve the element of profit and does not attract the TDS, hence requested to delete the addition. The Ld. A.R. further argued that even if it is presumed that job conversion expenses attract TDS the assessee has deducted the TDS on part amounts hence it should be considered that assessee has made short deduction but not

non deduction of tax at source. The Ld. A.R. argued that the short deduction of tax at source does not attract disallowance u/s 40(a)(ia) of the Act but non deduction of tax at source the disallowance u/s 40(a)(ia) of the Act therefore the Ld. A.R. submitted that in any case the assessing officer erred in making disallowance u/s 40(a)(ia) of the Act and the CIT(A) has rightly deleted the addition which required to be upheld.

Responding to the argument of the Ld. A.R. the D.R. argued that the case law was relied upon by the Ld. A.R. in respect of short deduction at source is not applicable in the assessee's case since the assessee has deducted the TDS on part payments but not deducted the rest of the payments, whereas the decision relied upon by the Ld. A.R. in the case of Hon'ble Kolkata High Court judgement reference to short deduction of tax at source. Ex. i.e. deduction of TDS @ 1% instead of 2%. It is not so in the case of the assessee. With regard to the amendment to section 40(a)(ia) of the Act the Ld. D.R. argued that it was effective from 1.4.2013 but not retrospective effect.

7. We have heard both the parties, perused the materials available on record and gone through the orders of the authorities below. During the previous year relevant to the assessment year 2007-08, the assessee has paid a sum of ₹ 4,83,71,049/- to M/s Aditya Spinners. As

per the profit & loss account enclosed along with the return of income, the assessee submitted that ₹ 43,71,049/- was conversion charges, which is a contract amount and the TDS was deducted. The remaining amount of ₹ 4,36,13,708/- was conversion expenses which was reimbursed to the contractor on actual basis hence TDS is not applicable. In fact, this was the actual expenses incurred by the contractor for executing the contract, which was reimbursed by the assessee. The fact regarding the payment of conversion charges and reimbursement of expenses was evidenced by the agreement entered by the assessee with M/s. Aditya Spinners Pvt. Ltd., which was also relied upon by the Ld. CIT(A). As per the job conversion agreement, the assessee required to reimburse the production cost, power, wages, consumables, packing, etc. Therefore, the Ld. A.R. argued that job conversion charges would not attract TDS. The assessee relied on the decision of Hon'ble ITAT, Hyderabad 'B' Bench in the case of ACIT, Circle-2(2), Hyderabad Vs. Louis Berger International Inc. in ITA Nos.1073/Hyd/2004, 1074/Hyd/2004, 720/Hyd/2005 and 721/Hyd/2005 dated 30.6.2010. The Hon'ble ITAT in the cited decision held that there is no profit element in the reimbursement of expenses, hence the reimbursement of expenditure received by the recipient does not form part of total income. Since the reimbursement of expenditure does not

form part of total income, the TDS does not attract in respect of the reimbursement of expenditure. For ready reference, we extract para Nos.21 to 24 of the order relied upon by the Ld. A.R as follows:

"21. We have also carefully gone through the judgement of the Delhi High Court in CIT Vs. Industrial Engineering Projects Pvt. Ltd. (1993) 202 ITR 1014. In the case before the Delhi High Court the assessee had agreement with M/s. ETAG, a Swiss Company, for rendering services. The assessee would receive a minimum sum of ₹ 1,20,000/- per month for the services rendered besides reimbursement of certain costs and expenditure incurred by the assessee while rendering the services as per the agreement. The Income-tax Officer disallowed the expenses incurred. On appeal by the assessee before the Delhi Bench of this Tribunal, it was held that the reimbursement of the expenditure did not constitute income as the expenses were incurred on behalf of the Swiss company. On a reference to the Delhi High Court at the instance of the Revenue, the Delhi High Court after considering the judgement of the Apex Court in the case of CIT Vs. Tejaji Farasram Kharawalla Ltd. (1968) 67 ITR 95 held that the reimbursable expenditure cannot form part of the taxable income. Accordingly it was held that the reimbursable expenditures are to be excluded from the total income. In view of this judgement of the Delhi High Court, in our opinion, the reimbursable expenditure received by the assessee for the purpose of rendering services cannot form part of the total income. Therefore, it has to be excluded.

22. We have also carefully gone through the judgement of the Calcutta High Court in CIT Vs. Sanderson & Morgaon (1970) 75 ITR 433. In the case before the Calcutta High Court a firm of solicitors received money from their clients. The question arose before the Calcutta High Court was whether the money received by the solicitors in the course of their professional activities would form part of the total income or not. The Calcutta High Court held that the money received by the solicitors was not revenue receipt. It was further held that when a solicitor received money from his clients he does not do so as a trading receipt but he receives the money from the principal in capacity as an agent. Therefore, the money received does not have any profit making quality. In this case also the money was received by the assessee on behalf of their clients for incurring the expenditure. Therefore, the money received did not have the profit making quality as held by the Calcutta High Court. In our opinion, this judgement of the Calcutta High Court also supports the case of the assessee.

23. We have also carefully gone through the judgement of the Apex Court in the case of CIT Vs. Tejaji Farasram Kharawalla Ltd. (1968) 67 ITR 95. The assessee before the Apex Court acted as a selling agent

of Ciba (India) Ltd. The assessee was entitled to commission of 12.5% on sales. Out of the 12.5%, 7.5% was treated as selling commission and 5% as compensation in lieu of contingency expenses which it had to meet. The question arise before the Apex Court was whether the 5% selling commission in lieu of the contingency expenditure would form part of the total income or not. The Apex Court held that 5% of the expenses in lieu of the contingency expenses was for the expenditure incurred in the performance of the duties of the respondent as selling agent. Therefore, it will not form part of the taxable income Accordingly, the same was exempt. In view of this judgement of the Apex Court, the reimbursable expenditure received by the assessee in pursuance to the agreement cannot form part of the taxable income Accordingly, the same has to be excluded.

24. We have also carefully gone through the judgement of the Bombay High Court in CIT Vs. Tanubai D. Desai (1972) 84 ITR 713. In the case before the Bombay High Court, the assessee was a practicing solicitor. In the course of carrying on his profession the assessee used to receive money from or on behalf of his clients. The money received was deposited by him in separate current account with Imperial Bank of India. Subsequently, the assessee withdrew a sum of ₹ 3.25 lakhs and placed the same in fixed deposit with Chartered Bank. The assessee renewed the account from time to time together with interest earned thereon. The assessee earned interest on the fixed deposit. The interest earned on the fixed deposit was not adjusted by apportioning it to different clients whose moneys were deposited in the bank account. The assessee did not show the interest in the return of income. The question arose before the Bombay High Court was whether the interest accrued in the fixed deposit with Chartered Bank was the income of the assessee or not. The Bombay High Court after elaborately examining the issue found that the moneys received by the solicitor from his clients are held by him in fiduciary capacity. Even the income received from such money must equally be held by the solicitor in a fiduciary capacity. What the solicitor actually does with the income, i.e., whether he appropriates it to himself or not is a matter of no consequence. If the solicitor appropriates the interest accrued on such deposit to himself that would amount to a breach of his fiduciary relationship and whatever may be the consequences in law would follow. But his unauthorized act of converting any part of the corpus or even the income derived therefrom would not convert those moneys held by him for his benefit. Accordingly, it was held that the interest income which was neither disclosed in the return of income nor adjusted to the clients was held to be not taxable. In the case before us the facts are almost similar. The assessee received the money as a reimbursement after incurring the expenditure. In the case before the Bombay High Court, the money was received by the solicitor in advance. In the case before us the money was received after incurring the expenditure by way of reimbursement. Therefore, the reimbursable expenditure received by the assessee cannot form part of the total income In view of the above discussion, in our opinion, the reimbursable

expenditure received by the assessee cannot form part of the total income. Therefore, we do not find any infirmity in the order of the lower authority. Accordingly, the same is confirmed."

8. The CIT(A) also observed that reimbursement of expenditure does not attract TDS, hence no addition required to be made u/s 40(a)(ia) of the Act. This view is supported by ITAT, Delhi Bench in the case of ACIT Vs. Modicon Network Pvt. Ltd. reported in (2007) 14 SOT 204 (2007) (Del). For ready reference, we extract the relevant portion of the order as under:

"Obligation to deduct tax under s. 195(1) is only with reference to the income element imbedded in the remittance. The obligation of the assessee to deduct tax under s. 195 is limited only to the appropriate proportion of income chargeable under the Act. It is therefore clear that any remittance which does not have an income element which is chargeable to tax need not suffer tax deduction at source.—Transmission Corporation of A.P. Ltd. &Anr. vs. CIT (1999) 155 CTR (SC) 489: (1999) 239 ITR 587 (SC) relied on.

(Para 12)

9. The Hon'ble ITAT Delhi relied on the decision of Transmission Corporation of India of AP Limited Vs. CIT 155 CTR (SC) 489. In the instant case, the expenditure debited to P&L account towards the conversion expenses is reimbursement of expenditure, which is supported by the agreement entered into by the assessee. The A.O. made addition u/s 40(a)(ia) of the Act but not given any reasoning. The Ld. CIT(A) held that the same is reimbursement of expenses. M/s. Aditya Spinners Limited has admitted the entire amount of reimbursement of expenses as well as conversion charges as income in

their hands and filed the return of income for the relevant assessment year. As held by the coordinate bench of Hyderabad in the case of M/s. Louis Berger International Inc. (supra) since no element of profit is involved, the reimbursement of expenditure does not form part of total income. Therefore we are of the considered view that the conversion expenses of Rs.4,36,13,708 was the reimbursement of expenditure and does not attract the TDS and consequent disallowance u/s 40a(ia). The Special bench decision in the case of Merylin Shipping has no application in view of Hon'ble Apex court's decision in the case of Palam gas.

In the assessee's case the recipient has admitted the entire receipt as income and filed the return of Income. Following the decision of coordinate bench in the case of B. Dwarakanatha Reddy Vs. DCIT in ITA Nos.703 & 704/Hyd/2015, dated 11/09/2015 we hold that provisions of section 40(a)(ia) of the Act are not applicable provided the payer has offered the amount for tax purpose and have paid or deemed to have paid the taxes on such income. Since the recipient has already has admitted the income and paid the taxes and the amount in question was reimbursement of expenses, we hold that the addition made by the A.O. u/s 40(a)(ia) of the Act is unsustainable and accordingly, we uphold the order of the Ld. CIT(A) and dismiss the revenue's appeal.

10. In the result, the appeal filed by the revenue is dismissed.

11. The assessee has filed cross objection supporting the orders of the CIT(A). Since the revenue's appeal has been dismissed, the cross objection filed by the assessee becomes infructuous and accordingly dismissed.

The above order was pronounced in the open court on 21st Feb'18.

Sd/-

(वी. दुर्गराव)

(V. DURGA RAO)

न्यायिक सदस्य/JUDICIAL MEMBER

Sd/-

(डि.एस. सुन्दर सिंह)

(D.S. SUNDER SINGH)

लेखा सदस्य/ACCOUNTANT MEMBER

विशाखापटणम /Visakhapatnam:

दिनांक /Dated : 21.02.2018

VG/SPS

आदेश की प्रतिलिपि अग्रेषित/Copy of the order forwarded to:-

1. अपीलार्थी / The Appellant – The ACIT, Circle-2(1), Guntur
2. प्रत्यार्थी / The Respondent – M/s. Veera Associates, 5-60-1/99, 4/4, Ashok Nagar, Guntur
3. आयकर आयुक्त / The CIT, Guntur
4. आयकर आयुक्त (अपील) / The CIT (A), Guntur
5. विभागीय प्रतिनिधि, आय कर अपीलीय अधिकरण, विशाखापटणम / DR, ITAT, Visakhapatnam
6. गार्ड फ़ाईल / Guard file

आदेशानुसार / BY ORDER

// True Copy //

Sr. Private Secretary
ITAT, VISAKHAPATNAM