

IN THE INCOME TAX APPELLATE TRIBUNAL  
“D” Bench, Mumbai  
Before S/Shri B.R. Baskaran (AM) & Sandeep Gosain (JM)

I.T.A. No. 3907/Mum/2013 (Assessment Year 2007-08)

M/s. De Beers India Pvt. Ltd. 83, Maker Chambers VI Nariman Point Mumbai-400 021. PAN : AAACD1900D (Appellant)	Vs.	DCIT 3(1) Mumbai  (Respondent)
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Assessee by	Shri Nitesh Joshi
Department by	Shri Ram Tiwari
Date of Hearing	3.4.2018
Date of Pronouncement	30.5.2018

O R D E R

Per B.R. Baskaran (AM) :-

The appeal filed by the assessee is directed against the order dated 19-03-2013 passed by Ld CIT(A)-6, Mumbai and it relates to the assessment year 2007-08. The assessee is aggrieved by the decision rendered by Ld CIT(A) on the following issues:-

- (a) Reallocation of Head office expenses
  - (b) Assessment of interest income under the head Income from other sources instead of assessing the same as business income.
  - (c) Assessment of sale of scrap as income under the head income from other sources income instead of assessing the same as business income.
2. The assessee is engaged in the business of exploration, prospecting and mining activities for diamonds and other minerals. It also provides consultancy services. During the year under consideration, the assessee declared Professional fee on consultation to the tune of Rs.207.19 lakhs, which was computed at cost plus mark up of 5%. The assessee had incurred expenses under various heads aggregating to Rs.2298.92 lakhs. Out of the above, the assessee disallowed a sum of Rs.1777.47 lakhs ascribing them

towards mineral prospecting activity. The amount so disallowed was capitalized and later amortised over a period of 10 years as per the provisions of sec.35E of the Act. The AO examined the expenses debited to Profit and Loss account and that was allocated to consultancy services. He noticed that the assessee has incurred various expenses at Head office (described as "Fixed costs") aggregating to Rs.198.17 lakhs and the same has been fully charged to the Profit and Loss account, i.e., no portion of head office expenses was allocated towards mineral prospecting activity or consulting activity. The AO took the view that various expenses incurred in the Head office should be allocated to Mineral Prospecting activity also, as the head office is functioning for entire business activities of the assessee. He noticed that ratio of expenses that were allocated between mineral prospecting activity and consultancy activity was in the ratio of 9:1. Accordingly, the AO allocated 90% of Head office expenses to the Mineral prospecting activity and 10% to consulting activity. Accordingly the AO disallowed 90% of the head office expenses with the observation that the assessee may amortise the same in 10 years as per the provisions of sec. 35E of the Act.

3. The AO noticed that the assessee has determined fee for consultancy services at cost plus mark up of 5%. Accordingly the AO included the head office expenses allocated to consultancy services (i.e., 10% of head office expenses) to the cost and accordingly re-computed income from consultancy services at 5% of the revised cost. Accordingly the consultancy income was also increased by the AO marginally.

4. The assessee had declared interest from bank deposits and sale of scrap as its business income. The AO assessed both the receipts as income under the head income from other sources.

5. The Ld CIT(A) also confirmed the order passed by the AO on the above said issues.

6. The first issue relates to the allocation of head office expenses to mineral prospecting activity. It was brought to our notice by the Ld A.R that identical issue of disallowance and allocation of common expenses to Mineral prospecting activity was examined by the Tribunal in the assessee's own case in AY 2005-06 in ITA No.6420/Mum/08. The Tribunal examined the provisions of sec. 35E of the Act and noticed that **the expenses which qualify for deduction u/s 35E are those expenses which are incurred wholly and exclusively on the operations relating to prospecting of minerals.** Accordingly the Tribunal has expressed the view that the expenses that are directly related to prospecting of diamonds and other minerals are required to be capitalized u/s 35E of the Act. Accordingly it was held that other indirect expenses incurred by the assessee in the nature of salaries of employees who are not working on prospecting work, administrative expenses, professional fee, rent, communication expenses, travelling expenses unconnected with the prospecting of minerals are not required to be capitalized u/s 35E of the Act. It was also brought to our notice that the decision rendered in AY 2005-06 has been followed in 2001-02 to 2003-04 in ITA Nos. 40/Mum/2006 and 6193 & 86/Mum/2007 dated 16-12-2011.

7. The Ld A.R submitted that the expenses incurred at the head office are indirect expenses and they are not connected wholly and exclusively for the purpose of prospecting of minerals. Accordingly he submitted that the decision rendered by the co-ordinate benches would squarely apply to the facts of the present case.

8. On the contrary, the Ld D.R submitted that the head office expenses were considered as direct expenses by the tax authorities.

9. We have heard rival contentions on this issue and perused the record. We notice from the assessment order that the assessee has explained that the head office expenses consist of (a) salary expenses paid to head office personnel like M.D, CFO, Secretary, Accounts assistant, telephone operator,

administrative staffs, peons etc; (b) administration expenses like property rental, travel expenses, telephone expenses, audit fees, depreciation, printing & stationery, courier charges, vehicle expenses etc. We further notice that the co-ordinate bench has considered very same expenses in AY 2005-06 and has held that these indirect expenses, which are not connected with the activity of prospecting of minerals, cannot be capitalized u/s 35E of the Act. From the orders of tax authorities, we notice that they have not identified any direct expenses connected with the activity of prospecting of minerals out of the Head office expenses. Unless such an exercise is undertaken, in our view, the head office expenses could not have been allocated to mineral prospecting activity. Accordingly, following the order passed by the co-ordinate bench in AY 2005-06, we set aside the order passed by Id CIT(A) on this issue and direct the AO to allow entire head office expenses debited to Profit and Loss account.

10. In view of the above, the re-working of consultancy income done by the AO also stands set aside.

11. The next issue relates to the assessment of interest income under the head income from other sources. The assessee earned interest from bank deposits of Rs.23.26 lakhs and offered the same under the head income from business. The AO assessed the same as income under the head income from other sources. We notice that the assessee has deposited surplus funds into the bank and earned interest income. As per the decision rendered by Hon'ble Supreme Court in the case of Tuticorin Alkali Chemicals & Fertilisers Ltd (227 ITR 172), the interest income earned on depositing of surplus funds is required to be assessed as income under the head income from other sources. In the case of Swani Spice Mills (P) Ltd (322 ITR 288), the Hon'ble Bombay High Court has expressed identical view. Hence we are of the view that the Ld CIT(A) was justified in confirming the assessment of interest income from bank deposits as income under the head income from other sources.

12. The next issue relates to the assessment of scrap sales of Rs.69,737/- as income under the head income from other sources. Since the scrap was generated from the business activities of the assessee, we are of the view that the revenue received from sale of scrap forms part of business receipts only. Accordingly we set aside the order passed by Ld CIT(A) on this issue and direct the AO to assess the income from sale of scrap under the head income from business.

13. In the result, the appeal filed by the assessee is partly allowed.  
Order has been pronounced in the Court on 30.5.2018.

Sd/-  
(SANDEEP GOSAIN)  
JUDICIAL MEMBER

Sd/-  
(B.R.BASKARAN)  
ACCOUNTANT MEMBER

Mumbai; Dated : 30/5/2018

Copy of the Order forwarded to :

1. The Appellant
2. The Respondent
3. The CIT(A)
4. CIT
5. DR, ITAT, Mumbai
6. Guard File.

//True Copy//

BY ORDER,

(Senior Private Secretary)  
ITAT, Mumbai

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