

**INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH "G": NEW DELHI**

**BEFORE SHRI BHAVNESH SAINI, JUDICIAL MEMBER
AND
SHRI O.P. KANT, ACCOUNTANT MEMBER**

ITA No.5349/Del/2015
Asstt. Year: 2011-12

Luthra & Luthra Law Offices , 103, Ashoka Estate, Barakhamba Road, New Delhi – 110 001.	Vs.	ACIT, Circle 37 (1), New Delhi.
(Appellant)		(Respondent)

Assessee by:	Shri Saksham Singhal & Shri Sumit Mangal, Advocate
Department by :	Shri S.S. Rana, CIT(DR)
Date of Hearing	30/01/2019
Date of pronouncement	12/02/2019

ORDER

PER O.P. KANT, A.M.

This appeal by the assessee is directed against order dated 07/08/2015 passed by the Ld. Commissioner of Income-tax (Appeals)-20, New Delhi [in short the Ld. CIT(A)] for assessment year 2011-12 raising following grounds:

"1. The order passed by the Learned Commissioner of Income Tax (Appeals) – XX ("CIT(A)") under section 250 of the Income Tax Act, 1961 ("the Act") is bad in law and on the facts and circumstances of the case.

2. The Ld. CIT(A) has erred in law and in the facts and circumstances of the case by upholding disallowance of Rs. 45,00,000 made by the Learned Asstt. Commissioner of Income Tax, Circle 37(1) ("Ld. AO") on account of remuneration paid to partners of the firm.

3. The Ld. CIT(A) has erred in law by ignoring the order passed by the Hon'ble Commissioner of Income Tax (Appeals) in the appellant's own case in Assessment Year 2009-10 deleting the disallowance of remuneration paid to the partners of the firm.

4. The above grounds of appeals are independent and without prejudice to one another.

5. The appellant craves leave to add /withdraw or amend any ground of appeal at the time of hearing."

2. In the above grounds of appeal, the solitary issue involved is of disallowance of Rs. 45,00,000/- on account of remuneration paid to partners of the firm.

3. The briefly stated facts of the case are that the assessee is a law firm (partnership) and derived income under the head "profit and gains of business & profession" and "income from other sources". The Assessing Officer in the assessment completed u/s 143(3) of the Income Tax Act, 1961 (hereinafter referred as the Act) on 29/03/2014 disallowed one of the amount as remuneration of Rs. 45,00,000/- paid to two partners namely Sh Rajiv K Luthra (Rs. 30,00,000/-) and Sh. Mohit Saraf (Rs.15,00,000/-) on the ground that same has not been paid in accordance with the provisions of section 40(b)(v) of the Act. The Assessing Officer noted that the partnership deed provided that the remuneration paid to all the partners will be the amount of

remuneration allowable u/s 40(b)(v) of the Act to be shared amongst themselves in their profit-sharing ratio in that year .

4. The Ld. Assessing Officer relying on the CBDT circular No. 739 dated 25/03/1996 ,observed that the CBDT has clarified that for the assessment year subsequent to AY 1996-97, no deduction u/s 40(b)(v) of the Act will be admissible unless the partnership deed either specifies the amount of remuneration payable to each individual working partner or lays down the manner of quantifying such remuneration. In view of the Assessing Officer, the partnership deed neither did quantify the amount of remuneration to partners nor specified the manner of quantifying such remuneration. Thus, the remuneration paid not being in accordance with the provisions of section 40(b)(v), not allowable . The Ld. Assessing Officer also relied on the decision of the Hon'ble Delhi High Court in the case of Sood Brij & Associate Vs. CIT (2010)15 taxmnn.com 76 (Delhi). The Ld. CIT(A) upheld the finding of the Ld. Assessing Officer. Aggrieved with the finding of the Ld. CIT(A), the assessee is in appeal before the Tribunal raising the grounds as reproduced above.

5. Before us, the Ld. Counsel of the assessee filed a paper book containing pages 1 to 93 and submitted that the assessee has paid remuneration to the partners in accordance with the provisions of section 40(b)(v) of the Act. The Ld. Counsel drawn our attention to the relevant clauses of the partnership deed and submitted that manner of the quantifying remuneration to partner has been duly specified. He further relied on the decision of the Hon'ble Delhi High Court in the case of CIT vs. Vaish Associates (2015) 63 taxmann.com 90 (Delhi) . He further submitted that remuneration paid by the firm to its partners was also disallowed by the Assessing Officer in assessment year 2009-10. However, the Ld. CIT(A) deleted the said addition and

the Department has not preferred any appeal on said issue before the Tribunal. According to the assessee, the order of Ld. CIT(A) in the year under consideration has been passed ignoring the principle of the consistency which is supported by plethora of decisions including Radhasoami Satsang Vs CIT (1992) 193 ITR 321 (SC). The Ld. Counsel also submitted that ratio of the decision of the Hon'ble Delhi High Court in the case of Sood Brij and Associates (supra) is not applicable over the facts of the instant case because in the said case remuneration was payable to future mutual agreements.

6. The Ld. DR on the other hand relied on the order of the lower authorities.

7. We have heard the rival submissions and perused the relevant material on record. In the instant case, the partnership firm has paid remuneration of Rs. 45,00,000/- to two partners in the ratio of 2/3 : 1/3. The relevant clause of the partnership deed dated 31.3.1999 of the assessee firm is reproduced by the Ld. Assessing Officer in the assessment order. For ready reference said Clause is reproduced as under:

“It is hereby agreed that all partners of the firm are working partners (RKL the Sr. Managing Partner) and would be required to perform such duties as are decided and allotted to them after due deliberation and discussions. The remuneration paid to all of the partners will be the amount of remuneration allowable under section 40(b)(v) of the Income Tax Act, 1961 to be shared amongst themselves in their profit sharing ratio in that year.”

8. The amount of allowability of remuneration to partners has been specified in section 40(b)(v) of the Act , which is reproduced as under :

“Notwithstanding anything to the contrary to sections 30 to [38J, the following amounts shall not be deducted in computing the income chargeable under the head "Profits and gains of business or profession ".

(v) any payment of remuneration to any partner who is a working partner, which is authorized by, and is in accordance with, the terms of the partnership deed and relates to any period falling after the date of such partnership deed in so far as the amount of such payment to all the partners during the previous year exceeds the aggregate amount computed as hereunder :-

<i>[(a) on the first Rs. 3,00,000 of the book-profit or in case of a loss</i>	<i>Rs 1,50,000 or at the rate of 90 per cent of the book-profit, whichever is more;</i>
<i>(b) on the balance of the book-profit</i>	<i>At the rate of 60 per cent:</i>

Provided that in relation to any payment under this clause to the partner during the previous year relevant to the assessment year commencing on the 1st day of April, 1993, the terms of the partnership deed may, at any time during the previous year, provide for such payment.”

9. The contention of the Assessing Officer is that the CBDT in circular No. 739 dated 25/03/1996 has clarified the position of the salary/remuneration paid to partners as provided u/s 40(b)(v) of the

Act. The Ld. Assessing Officer observed that the remuneration to the partners should either be quantified or manner of the quantification should be specified. Contents of the relevance circular are reproduced as under:

Circular No. 739 dated 25/03/1996

“The Boards have received representations seeking clarification regarding disallowance of remuneration paid to the working partners as provided u/s. 40(b)(v) of the IT Act. In particulars, the representations have referred to two types of clauses which are generally incorporated in the partnership deeds. These are:

- i. The partners have agreed that the remuneration to a working partners will be the amount of remuneration allowable under the provision of section 40(b)(v) of the IT Act; and*
- ii. The amount of remuneration to working partner will be as may be mutually agreed upon between partners at the end of the year.*

It has been represented that the A.Os are not allowing deduction on the basis of these and similar clauses in the course of scrutiny assessments for the reason that they neither specify the amount of remuneration to each individual nor lay down the manner of quantifying such remuneration.

2. The Board have considered the representations. Since, the amended provisions of section 40(b) have been introduced only with effect from the A.Y.1993-94 and these may not have been understood correctly the Board are of the view that a liberal approach may be taken for the initial years. It

has been decided that for the A.Y. 1993-94 to 1996-97 deduction for remuneration to a working partner may be allowed on the basis of the clauses of the type mentioned at 1(i) above.

3. In case where neither the amount has been quantified nor even the limit of total remuneration has been specified but the same has been left to be determined by the partners at the end of the accounting period, in such cases payment of remuneration of the firm's income.

4. It is clarified that for the assessment year subsequent to the A.Y. 1996-97, no deduction u/s. 40(b)(v) will be admissible unless the partnership deed either specifies the amount of remuneration payable to each individual working partner or lays down the manner of quantifying such remuneration. "

10. According to Assessing Officer in above clause of the partnership which is reproduced in para 7 of this order, the remuneration has neither been quantified nor manner of quantification has been specified. However in our opinion, the finding of the Ld. Assessing Officer as well as Ld. CIT(A) on this issue is not correct. The partnership deed has specified that the amount of remuneration allowable u/s 40(b)(v) would be the amount of remuneration paid to the partners and same would be shared in their profit-sharing ratio in that year. The profit-sharing ratio of the partners has been specified as 2/3rd (Sh Rajiv K Luthra) and 1/3rd (Sh Mohit Saraf). The assessee accordingly paid total remuneration of Rs. 45,00,000/-in the profit-sharing ratio to both the partners. In our view, the clause of the partnership deed satisfies the requirement of the CBDT circular

(supra) and there is no violation on the part of the assessee in this regard.

11. Further the ratio in the case of Sood Brij & associates (supra) also does not apply in the case of the assessee as in the said case, according to the partnership deed, the remuneration to partners was left to payable for future mutual agreement, whereas in the instant case remuneration has been paid in the profit-sharing ratio of the partners. The relevant part of the decision is reproduced as under:

“(Paragraph 7 & 8)

Clauses 7 of the partnership deed dated 1st May, 1976 reads as under:-

"7. That the profits or losses of the partnership, as the case may be, shall be divided amongst and borne by the partners equally. "

8. Clauses 1 and 2 of the supplementary partnership deed dated 1st April, 1992 read:

"That subject to mutual consent of the partners, and subject to the provisions of the Income Tax Act, 1961, the working partner or partners shall be paid such remuneration as may be mutually agreed between themselves, from time to time, and such remuneration shall be deductible expense before arriving at the share of the partners as allocable from the net profits.

That both the partners (hereinafter referred as working partners), shall devote their time and attention in the conduct of the affairs of the partnership firm, as the circumstances and need of the firms business may require. The total remuneration payable to the working partners shall be an amount permissible as remuneration

to the working partners under the Income Tax Act, 1961 and as applicable from time to time. "

[Paragraph 13 and 14]

Ratio of the decision of the Himachal Pradesh High Court in CIT v. Anil Hardware Store [2010} 323 ITR 368, does not assist the stand and contention of the appellant. On examining the partnership deed, it was held that the two partners were entitled to 50% or equal amount as remuneration. The contention of the Revenue that the partnership deed did not exactly determine the remuneration payable to the partners, was rejected holding that the requirement of the section was that the partnership deed should specify the amount payable or that the manner of quantifying the remuneration should be specified. In the said case, the High Court held that the manner of fixing the remuneration was specified in the partnership deed.

On reading the supplementary partnership deed, it is clear that the remuneration is not specified. The manner of quantifying the remuneration is not specified. On the other hand, the remuneration payable is left to future mutual agreement between the partners who are entitled to decide and quantify the quantum. Remuneration can be any amount or figure but not more than the maximum amount stated in section 40(b)(v). Therefore, the requirements of section 40(b)(v) are not satisfied."

12. The Ld. Counsel has also relied on the decision of the Hon'ble Delhi High Court in the case of Vaish Associates (Supra). The relevant part of the decision is reproduced as under:

"[8} Having heard the submissions of Ms. Suruchi Aggarwal, learned Senior Standing counsel for the Revenue and Ms. Kavita

Jha, learned counsel for the Respondent Assessee, the Court finds no reason to take a view different from the one taken by the ITAT in the facts and circumstances of the case. Clause 6(a) of the partnership deed dated 20th June 2008 clearly indicates the methodology and the manner of computing the remuneration of partners. The remuneration of the partners has been computed in terms thereof The Court additionally notes that under Section 28(v) of the Act, any salary or remuneration by whatever name called received by partners of a firm would be chargeable to tax under the head profits and gains of business or profession. The proviso to Section 28 (v) states that where such salary has been allowed to be deducted under Section 40(b)(v), the income shall be adjusted to the extent of the amount not so allowed to be deducted. Further Section 155 (1A) of the Act states that where in respect of a completed assessment of a partner in a firm, it is found on the assessment or reassessment of the firm that any remuneration to any partner is not deductible under Section 40(b), the AO may amend the order of the assessment of the partner with a view to adjusting the income of the partner to the extent of the amount not so deductible. A conspectus of these provisions makes the opinion the ITAT consistent with the legal position.

[9] Consequently, the Court finds no legal infirmity in the interpretation placed by the ITAT on Clause 6(a) of the partnership deed dated 22nd June 2008 to conclude that the salary paid to the partners was in accordance with Section 40(b)(v) of the Act and ought not to have been disallowed. Consequently, as regards this issue, no substantial question of law arises.”

13. In the above case the partners were entitled to annual salary equivalent with percentage of profit multiplied by the allocable profit

calculated as per the provisions of section 40(b)(v) of the Act. In the instant case also remuneration has been shared in the profit-sharing ratio.

14. The issue in dispute also deserve to be allowed on the principle of consistency as identical disallowance has been deleted by the Ld. CIT(A) immediately preceding assessment year i.e. 2009-10 and no appeal has been preferred by the Department on the said issue before the Tribunal.

15. In view of the aforesaid discussion and, respectfully following the decision of the Hon'ble Delhi High Court in the case of Vaish Associates (supra), we set aside the finding of the lower authorities on the issue in dispute and direct the Assessing Officer to delete the disallowance. All the grounds of appeal of the assessee are accordingly allowed.

16. In the result, the appeal of the assessee is allowed.

This decision was pronounced in the Open Court on 12th February, 2019.

sd/-
(BHAVNESH SAINI)
JUDICIAL MEMBER

sd/-
(O.P. KANT)
ACCOUNTANT MEMBER

Dated: 12/02/2019

Veena

Copy forwarded to

1. Applicant
2. Respondent
3. CIT
4. CIT (A)
5. DR:ITAT

ASSISTANT REGISTRAR
ITAT, New Delhi