आयकर अपीलीय अधिकरण, अहमदाबाद न्यायपीठ

IN THE INCOME TAX APPELLATE TRIBUNAL,
'' A" BENCH, AHMEDABAD

BEFORE SHRI RAJPAL YADAV, VICE PRESIDENT
And
SHRI WASEEM AHMED, ACCOUNTANT MEMBER

आयकर अपील सं./**ITA No. 1135/AHD/2017**
निर्धारण वर्ष/Asstt. Year: 2012-2013

Virmati Software & Telecommunication Limited, A-2/3, Arjun Tower, Satellite Road, Satellite, Ahmedabad-380 015. **PAN: AAACV6480G**	Vs.	D.C.I.T, Cirle-4(1)(2) Ahmedabad.

(Applicant)		**(Respondent)**

Assessee by	:	Shri Bandish Soparkar, A.R
Revenue by	:	Shri Deelip Kumar, Sr.D.R

सुनवाई की तारीख/**Date of Hearing : 23/01/2020**
घोषणा की तारीख /**Date of Pronouncement: 05/03/2020**

आदेश/O R D E R

PER WASEEM AHMED, ACCOUNTANT MEMBER:

The captioned appeal has been filed at the instance of the Assessee against the order of the Learned Commissioner of Income Tax (Appeals)-1, Ahmedabad, dated 27/02/2018 (in short "Ld. CIT(A)") arising in the matter of assessment order passed under s.143(3) r.w.s. 254 of the Income Tax Act, 1961 (here-in-after referred to as "the Act") dt.28/03/2016 relevant to the Assessment Year 2009-2010.

The assessee has raised following grounds of appeals

1. *The Learned CIT(A) has grossly erred in law and on facts of the case in confirming the disallowance of interest expenditure of Rs.5,00,000/- out of total disallowance of Rs.9,97,000/- made by the Id. AO u/s 36(l)(iii) of the Act.*

2. *The Learned CIT(A) has grossly erred in law and on facts of the case in confirming the action of Id. AO in not granting Foreign Tax Credit of Rs.21,88,147/- as claimed by the Appellant u/s 91 of the Act.*

3. *Both the lower authorities have passed the orders without properly appreciating the fact and that they further erred in grossly ignoring various submissions, explanations and information submitted by the appellant from time to time which ought to have been considered before passing the impugned order.*

4. *The learned CIT(A) has erred in law and on facts of the case in confirming action of the Id. AO in levying interest u/s 234A/B/C of the Act.*

5. *The learned CIT(A) has erred in law and on facts of the case in confirming action of the Id. AO in initiating penalty u/s 271(l)(c) of the Act.*

The appellant craves leave to add, amend, alter, edit, delete, modify or change all or any of the grounds of appeal at the time of or before the hearing of the appeal.

2. The 1st issue raised by the assessee is that the learned CIT-A erred in confirming the part disallowance of interest expenses for Rs. 5 lakh out of the total disallowance of Rs. 9,97,000/- made by the AO on account of diversion of interest-bearing fund under section 36(1)(iii) of the Act.

3. The facts as culled out from the orders of the authorities below are that the assessee in the present case is a public limited company and engaged in the business of customized software development and maintenance. The assessee in the year under consideration has made investment in the office space for Rs. 2,43,00,000/- only. The payment for such investment was made by the assessee from the HDFC OD account. However the assessee during the assessment proceedings claimed that, it has sufficient own fund exceeding the amount of investment.

3.1 However, the AO disbelieved the contention of the assessee by observing that the assessee has not furnished day to day fund flow statements to justify that the borrowed fund has not been diverted for the impugned investments. Accordingly

the AO determined the amount of interest relatable to such investments for Rs.9,97,000/- being 12% of the amount of investment and added to the total income of the assessee.

Aggrieved assessee preferred an appeal to the learned CIT (A).

4. The assessee before the learned CIT (A) submitted that, it has received fund from the debtors in its current account maintained with the assessee bank which was subsequently transferred to the HDFC OD account. The assessee also claimed to have realized a sum of Rs. 3.70 crores from the debtors which is more than the investments. Thus the assessee claimed that it has not made any investments out of the borrowed fund as alleged by the AO.

5. However, the learned CIT (A) found that the assessee is using common bank account for its borrowed funds for its business transactions. As such the investment was made by the assessee out of its mixed fund. Accordingly the learned CIT (A) was of the view that the possibility for diverting the borrowed fund for the impugned investments cannot be ruled out as the assessee did not maintain separate accounts. Accordingly, the learned CIT (A) confirmed the addition of Rs. 5 lakh out of the total addition made by the AO. Hence the learned CIT (A) partly confirmed the addition made by the AO.

Being aggrieved by the order of the learned CIT (A), the assessee is in appeal before us.

6. The learned AR before us filed a paper book running from pages 1 to 114 and submitted that its own funds exceeds the amount of investment as evident from the financial statements placed on pages 8 to 21 of the paper book. Accordingly, the learned AR claimed that it can be presumed that the investment was made out of the interest free fund of the assessee.

7. On the other hand, the learned DR vehemently supported the order of the authorities below.

8. We have heard the rival contentions of both the parties and perused the materials available on record before us. Admittedly, the own fund of the assessee as on 31st March 2012 was excess to the amount of investment as evident from the Balance Sheet of the assessee placed on page 8 of the paper book. The relevant extract of the audited financial statement stands as under:

Particulars	*Note No.*	*As on 31st march 2012*		*As on 31st march 2011*	
		Rs.	*Rs.*	*Rs.*	*Rs.*
1. EQUITY AND LIABILITIES					
1.Shareholder's funds					
	1	*48,450,000.00*		*48,450,000.00*	
a.Share capital	*2*	*17,727,486.13*		*13,376,310.55*	
b.Reserves and surplus			*66,177,486.13*		*61,826,310.55*

In view of the above, it can be presumed that the investment was made by the assessee for Rs. 2.43 crores out of its own funds despite the fact that the payment was made by the assessee out of the HDFC OD account as discussed above. In holding so we place our reliance on the judgment of the Hon'ble Gujarat High Court in the case of CIT vs. Amod Stamping (P.) Ltd. reported in 45 Taxamnn.com 427 wherein it was held as under:

> *In the case of Reliance Utilities & Power Ltd. (supra), the Bombay High Court has held that if there are funds available both interest-free and overdraft and/or loans taken, then a presumption would arise that investments would be out of the interest-free funds generated or available with the company, if the interest-free funds were sufficient to meet the investments and therefore, interest was deductible. Similar view has been taken by the Division Bench of this Court in the case of CIT v. Gujarat State Fertilizers & Chemicals Ltd. [2013] 358 ITR 323/36 taxmann.com 230/217 Taxman 229 (Guj.). Applying the ratio/law laid down by the Bombay High Court in the case of Reliance Utilities & Power Ltd. (supra) as well as Division Bench of this Court in the case of Gujarat State Fertilizers & Chemicals Ltd. (supra) to the facts of the case on hand and when it has been found that the assessee was having interest-free funds far in excess of investments and therefore, it can be said that the investments are made out of interest-free funds and therefore, the AO was not justified in making additions and/or making disallowance under section 36(1)(iii) of the IT Act. Under the circumstances, no error and/or illegality has been committed by the learned ITAT in deleting the disallowance made by the AO under section 36(1)(iii) of the IT*

Act. No question of law much less substantial question of law arise with respect to deletion of the disallowance made by the AO under section 36(1)(iii) of the IT Act.

8.1 The principles laid down by the Hon'ble Gujarat High Court in the case as discussed above are squarely applicable to the present facts of the case. Accordingly, we do not find any reason to uphold the finding of the learned CIT (A). Therefore, we direct the AO to delete the addition made by him. Hence the ground of appeal of the assessee is allowed.

9. The next issue raised by the assessee is that the learned CIT-A erred in disallowing the claim of the assessee for foreign tax credit of Rs. 21,88,147.00 under the provisions of section 91 of the Act.

10. The assessee has shown income of Rs. 3,32,67,540.00 from the foreign parties based in Afghanistan for the software services rendered to them. These foreign parties deducted TDS for Rs. 23,17,075.00 being 7% of the income received by the assessee. Accordingly the assessee claimed that it has paid the taxes on the foreign income at the rate of 7% whereas the rate of income tax in India is 30.90% the income. As per the assessee, it is entitled for the relief under section 91 of the Act, with respect to doubly taxed income for the entire amount of TDS deducted in the foreign country being lower rate of tax in the said country.

10.1 The assessee also submitted that provision of section 91 of the Act have referred the income and not overseas net profit, net income or proportionate income. Therefore the rate of tax in the foreign country should be worked out after considering the gross receipts and the amount of TDS deducted which comes out at 7% which is lower than the rate of tax in India. Accordingly the assessee claimed the foreign tax credit of Rs. 23,17,075.00 under section 91 of the Act.

10.2 However, the AO disagreed with the contention of the assessee by observing that the tax in the foreign country cannot be applied to the amount of gross receipts. As such, the amount of income which is getting tax twice should be worked out for

determining the rate of tax in the foreign country and the same needs to be compared with the rate of tax in India. Accordingly the AO held that the expenses incurred by the assessee against the gross income from foreign countries needs to be adjusted for determining the rate of tax in the foreign country. But the assessee has not furnished the detailed computation of allowable tax credit of foreign countries.

10.3 The AO further found that the assessee has already incurred expenses in India and abroad for the income in India and abroad which have already been claimed by the assessee in the return of income. As per the AO the assessee has shown gross receipts including the receipts from the foreign countries in its profit and loss account amounting to Rs. 14,65,12,527.00 against which it has declared taxable profit at Rs. 81,58,136/- and thus determined the tax liability at Rs. 25,00,865/- only under the normal computation of income. The AO accordingly held that the taxable income shown by the assessee are constituting 5.56% of the gross receipts on which it is paying the tax at the rate of 30.90% in India. Thus the AO further held that whole of the gross receipt of the assessee are not made subject to tax in India. It is only profit of the company i.e. 5.56% in the above receipts which is being taxed in India. Accordingly the AO applying the same ratio with respect to the gross receipts generated from the foreign countries and worked out the doubly taxed income at Rs. 18,52,409.00 being 5.56% of 3,32,67,540.00. Thus the AO determined the allowable tax credit under section 91 of the Act in the manner as given below:

Indian rate of tax =India Income Tax / Total income = 25,20,865 / 81,58,140 =30.89%

Rate of tax of foreign country =Tax Deducted / Income assessed in that country = 23,17,075 / 3,32,67,540 =6.96%

Doubly taxed income =81.58,136 / 14,65,12,527 X 3,32,67,540

=18,52,409/-

(By applying same ratio of profit percentage i.e 5.56% on which assessee has paid taxes here)

Allowable credit= 18,52,409 X 6.96% = 1,28,928/- (By applying the lower of the two tax rates i.e 6.96% or 30.9% on the profit element of the receipts from Afghanistan) In view of the above the allowable foreign tax credit out of the tax withheld in Afghanistan is Rs.1,28,928/- only. Therefore the excess tax credit claimed by assessee of Rs.21,88,147/- - (23,17,075 – 1,28,928) is hereby disallowed in view of the provisions of section 91 of the Act.

Aggrieved assessee preferred an appeal to the learned CIT (A)

11. The assessee before the learned CIT (A) submitted that the gross foreign income which is being taxed in India should only be considered as doubly taxed income and not the element of profit on which tax has been paid.

12. However, the learned CIT (A) disregarded with the contention of the assessee by observing that the relief under section 91 of the Act is available to the assessee with respect to the doubly taxed income. The doubly taxed income shall be construed with respect to the net amount of receipts i.e. gross receipts minus the expenses. Thus the learned CIT (A) confirmed the order of the AO.

Being aggrieved by the order of the learned CIT (A), the assessee is in appeal before us.

13. The learned AR before us submitted that the assessee has paid the tax in the foreign country @ 7% which is less than the rate of tax in India. Therefore, the assessee should be given relief for the entire amount of tax paid in the foreign country. The learned AR in support of his contention placed his reliance on the order of Mumbai Tribunal in the case of Hindustan Construction Co. Ltd versus DCIT reported in 25 SOT 359.

The learned AR alternatively also contended that if the tax credit is not allowed to the assessee then the same should be allowed as an expense under section 37(1) of the Act. The learned AR in support of his contention relied on the judgment of Hon'ble Bombay High Court in the case of Reliance Infrastructure Ltd versus CIT reported in 390 ITR 271 .

14. On the other hand the learned DR before us submitted that the assessee is not entitled for the relief under section 91 of the Act with respect to the TDS deducted by the parties based in the foreign countries. As per the learned DR, there can be a possibility that the assessee has claimed the refund against such TDS certificate in the foreign country. As such the assessee has not brought anything on record evidencing that it has paid the taxes in the foreign country. The learned DR vehemently supported the order of the authorities below.

15. We have heard the rival contentions of both the parties and perused the materials available on record before us. The assessee in the present case has earned income from the foreign country namely Afghanistan on which the TDS was deducted by the foreign parties. The assessee accordingly claimed that it has paid taxes in the foreign country at the rate of 7% which is less than the rate of tax in India. Thus the assessee claimed that it is eligible for the tax relief under section 91 of the Act with respect to the entire amount of TDS deducted by the foreign parties. However, the AO disagreed with the contention of the assessee by observing that the rate of tax can be worked out against the net receipts of the income and not based on gross receipts as claimed by the assessee. Accordingly, the AO worked out the proportionate amount of tax with respect to foreign income amounting to Rs. 1,28,928 which is eligible for tax relief under section 91 of the Act. The view taken by the AO was subsequently confirmed by the learned CIT (A).

15.1 The controversy before us arises in the given facts and circumstances whether rate of tax in foreign country needs to be determined after considering the gross receipts or the net receipts/profit embedded in such gross receipts. To our mind the explanation (iii) to section 91 of the Act provides mechanism for determining the rate of tax in the foreign country. It requires that the income tax/super tax actually paid in the foreign country as per the laws prevailing therein and dividing the same by the whole amount of income as assessed in the foreign country. The relevant extract of the clause (iii) to explanation of section 91 of the Act reads as under:

Explanation.—In this section,—
*(i) ************
*(ii) **********
(iii) the expression "rate of tax of the said country" means income-tax and super-tax actually paid in the said country in accordance with the corresponding laws in force in the said country after deduction of all relief due, but before deduction of any relief due in the said country in respect of double taxation, divided by the whole amount of the income as assessed in the said country;

15.2 From the above, it is revealed that the amount of tax/super tax needs to be divided by the whole amount of income to work out the rate of tax. The word used whole amount of income denotes the income which signifies after the expenses. The word gross receipts have not been used therein. Even under the normal parlance, the income denotes only to the net profit i.e. gross receipts minus the expenses. Thus in our considered view, it is the only profit which should be considered while determining the rate of tax in the foreign country and the same needs to be compared with the rate of tax in India.

15.3 In the case on hand, we also note that the assessee has not given any working about the expenses incurred in the foreign country against the gross receipts. Thus in the absence of sufficient details, the AO had no alternate except to work out the proportionate amount of income eligible for relief under section 91 of the Act. Accordingly we do not find any infirmity in the order of the authorities below.

15.4 However Before parting, we note that there is force in the alternate argument of the learned AR for the assessee claiming for the deduction of the taxes paid in the foreign country as expenditure under section 37(1) of the Act. The amount of tax paid in a foreign country which is not eligible for benefit under section 91 of the Act, is expenditure eligible for deduction under section 37(1) of the Act. It is because such tax was paid in the course of the business and the corresponding business receipts were made to tax in India. In holding so we draw support and guidance from the judgment of Hon'ble Bombay High Court in the case of Reliance Infra Structure Ltd. vs. CIT reported in 390 ITR 271 wherein it was held as under:

> *Therefore, to the extent the payment of tax in Saudi Arabia on income which has arisen/accrued in India has to be considered in the nature of expenditure incurred or arisen to earn income and not hit by the provisions of Section 40(a)(ii) of the Act.*

In view of the above we hold that the assessee is eligible for deduction for the amount of foreign tax credit which was not allowed as tax relief under section 91 of the Act. Hence the ground of appeal of the assessee is partly allowed.

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

Order pronounced in the Court on 05/03/2020 at Ahmedabad.

-Sd-	**-Sd-**
(RAJPAL YADAV)	**(WASEEM AHMED)**
VICE PRESIDENT	**ACCOUNTANT MEMBER**

(True Copy)

Ahmedabad; Dated 05/03/2020

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