

**IN THE INCOME TAX APPELLATE TRIBUNAL
“F” BENCH, MUMBAI**

**BEFORE SHRI C. N. PRASAD, JM &
SHRI S. RIFAUR RAHMAN, AM**

आयकरअपीलसं./ I.T.A. No. 633/Mum/2019
(निर्धारणवर्ष / Assessment Year: 2012-13)

M/s Vishwaroop Infotech Pvt. Ltd. (now merged with M/s Wadhwagroup Holdings Pvt. Ltd.) 301, 3 rd floor, Platina, Plot-C-59, G Block, Bandra Kurla Complex, Bandra East, Mumbai-400 098	बनाम/ Vs.	ACIT Cen. Cir. – 5(4), Mumbai, Pin-
स्थायीलेखासं ./जीआइआरसं ./PAN No. AABCV8153D		
(अपीलार्थी/ Appellant)	:	(प्रत्यर्थी / Respondent)

अपीलार्थीकीओरसे/ Appellant by	:	Shri Jitendra Jain, AR
प्रत्यर्थीकीओरसे/ Respondent by	:	Ms. Samatha M, DR
Virtual Date of Hearing	:	15.10.2020
Date of Pronouncement	:	06.11.2020

आदेश / ORDER

Per S. Rifaur Rahman, Accountant Member:

The present appeal has been filed by the assessee against the order of Ld. Commissioner of Income Tax (Appeals) - 53 in

short referred as 'Ld. CIT(A)', Mumbai dated 19.11.2018 for Assessment Year (in short AY) 2012-13.

2. The brief facts of the case are, assessee is a company engaged in the business of leasing the commercial properties to earn lease rentals and for capital appreciations and also maintaining properties. The return of income declaring total income of Rs. 26,78,27,560/- was filed by the assessee on 30.09.2012. Thereafter, assessee has filed revised return of income on 29.03.14 declaring income at Rs. 26,90,54,370/-. The return was processed u/s 143(1) of the Act and subsequently, the case was selected for scrutiny and notices u/s 143(2) and 142(1) were issued and served on the assessee. In response, AR of the assessee filed the relevant information as called for.

3. With regard to disallowance u/s 14A r.w.r. 8D of the Act, it was explained that the assessee company is a partner in partnership firm namely M/s Vijay Associates (Wadhwa). The share of profit has been claimed as exempt u/s 10(2A) of the Income Tax Act, 1961. It has not incurred any expenses for making investment in partnership firm and has made the strategic

investment with the sole object to expand its business activities. The administrative expenses and interest expenses were incurred for carrying out its business activity and no part of the expenses can be considered as relatable to earning of exempt income. It was further submitted that out of total interest claimed in P&L A/c, a part of interest expenditure claimed u/s 24(b) under the head "Income from House Property" and balance interest claimed as trading expenses while calculating business income. Since no interest expenditure claimed in P&L account, therefore no disallowance u/s 14A can be made.

4. After considering the submission of assessee, AO rejected the submission of assessee. He observed that assessee cannot earn exempt income without systematic management of its investment portfolio. Investment decisions are very complex in nature. It requires substantial market research, day to day analysis of market trends and decisions with regard to acquisition, retention and sale of share at the most appropriate time. It would be, therefore, no proper to say that exempt income can be earned by incurring no or nominal expenditure. It is difficult to accept that an assessee can earn exempt income

without incurring any expenses whatsoever including management or administrative expenses as investment decisions are generally taken in a planned manner. The term "expenditure" occurring in section 14A would take in its sweep not only direct expenditure but also all forms of expenditure regardless of whether they are fixed, variable, direct, indirect, administrative, managerial or financial. In this regard, AO referred the judicial pronouncements wherein it was held that all expenses connected with the exempt income have to be disallowed u/s 14A regardless of whether they are direct or indirect, fixed or variable and managerial or financial in accordance with law. Further, AO observed that the expenditure incurred in relation to income which does not form part of the total income under the Act, has to be computed. For the year under consideration, the assessee cannot claim that the interest expenses were incurred entirely for his trading activity. These funds were also utilized for investment activity and the assessee cannot change the nature of expenses as per his convenience. Therefore, AO concluded that assessee has not brought anything on record to prove that he has not incurred expenses for earning of exempt income, accordingly provision of

section 14A r.w.r. 8D are very much applicable in this case and disallowed Rs. 1,47,97,219/-.`

5. With regard to rental income, assessee explained that he had entered into rental agreement with M/s Spanco BPO Services Ltd. The said company had made payment of rent as well as reimbursement of electricity up-to the financial year 2009-10 regularly. Thereafter, the said tenant (M/s Spanco BPO Services Ltd) did not make any payment due to financial constrains. Only a part payment of reimbursement of electricity and outstanding opening balance was paid by M/s Spanco BPO Services Ltd. Ultimately, M/s Spanco BPO Services Ltd vacated the premises in November 2011. The assessee has further submitted that though M/s Spanco BPO Services Ltd has made TDS & deposited the same into Government Account, but no rent has been received by the assessee. Therefore the assessee has not disclosed such rental income in the return of income. The assessee has also taken support of Rule 4 of Income tax Rules 1962 for unrealized rent.

6. From the above submission of assessee, AO has rejected the submission of assessee with the following observations:-

1. The assessee is following Mercantile method of accounting, therefore income has to be disclosed on accrual basis.
2. The deductor is deducting tax at source at the time of crediting the amount of rent and depositing the same into Government Account.
3. The assessee company has duly taken into account the claim of TDS in the return of income.
4. The assessee has taken support of Rule 4 of the I.T Rule 1962 for not disclosing the rental income. Rule 4 of the I.T Rule 1962 is being re-produced hereunder :-

(a) The tenancy is bona fide;

(b) The defaulting tenant has vacated, or steps have been taken to compel him to vacate the property;

(c) The defaulting tenant is not in occupation of any other property of the assessee;

(d) The assessee has taken all reasonable steps to institute legal proceedings for the recovery of the

unpaid rent or satisfied the Assessing Officer that legal proceedings would be useless.

7. AO further observed that though the assessee fulfils the first 3 conditions of Rule 4 of I.T Rule 1962, but has failed to fulfill the 4th condition. The assessee has neither furnished any documentary evidences for instituting any legal proceedings against the tenant for recovery of outstanding rent, nor proved that institution of legal proceedings would be useless. Therefore, AO concluded that the assessee has failed to disclose the rental income to the extent of Rs. 3,85,85,341/- in the return of income, accordingly added the same to the total income of assessee and initiated penalty proceeding u/s 271(1)(c) of the Act for furnishing inaccurate particulars /concealing true particulars of income.

8. Aggrieved with the above order, assessee preferred the appeal before Ld. CIT(A) and reiterated the same arguments as were raised before AO. Ld. CIT(A) after considering the detailed submission submitted by assessee, sustained the order of AO and rejected the contention of the assessee in respect of disallowance u/s 14A r.w.r. 8D and rental income.

9. Aggrieved with the above order, assessee is in appeal before us on the grounds mentioned below:-

1. i) The Commissioner of Income Tax(Appeals) - 53, Mumbai erred in confirming the addition of Rs.3,85,85,341/- made by the AO, being unrealized rent receivable from licensee M/s. Spanco BPO Services Pvt. Ltd and M/s Spanko Respondez BPO Private Limited.(hereinafter referred to as SPANKO)

Your Appellant submits that it has not received any rent from these Licensees and hence no income is offered to tax.

ii) The CIT(A) erred in confirming the addition of said rental income made by the AO solely on the ground that the licensees had deducted TDS on the unrealized rent which is reflected in the ITS Data and holding that the rental income ought to have been offered to tax by the Appellant.

iii) The CIT(A) erred in directing the AO to bring to tax the security deposit retained by the Appellant on vacation of premises without appreciating that the security deposit is to be adjusted against the outstanding rent receivable from Spanko.

2. (i) *The CIT(A) erred in confirming the disallowance u/s 14A of the Act to the extent of Rs.43,97,356/- (i.e.56% of Rs.78,52,422/-) as expense attributable to investment activity giving rise to the exempted income.*

The Appellant submits that it has not incurred any expenditure attributable to investment activity giving rise to the exempted income and hence no disallowance u/s 14A of the Act is called for. The Appellant made administrative expenses for carrying on its business activity and hence the same shall not be considered while calculating disallowance as per Section 14A r.w.r 8D (iii) of the I.T.Rules.

(ii) The CIT(A) erred in confirming disallowance of Rs.43,97,356/- (i.e.56% of Rs.78,52,4227-) u/s 14A of the Act which is excessive considering the facts and circumstances of the case of the Appellant.

(iii) The CIT(A) erred in confirming disallowance u/s 14A r.w.r. 8D(iii) without appreciating that the administrative expenses are incurred by the Appellant for carrying on its day to day business activity and none of the expenditure are incurred or related to carrying on of business of the partnership firm in which the Appellant is partner and hence no disallowance is called for u/s 14A of the Act.

Your Appellant craves leave to add, to alter or to

amend the aforesaid grounds of appeal.

10. At the time of hearing, Ld. AR appearing on behalf of the assessee submitted with regard to rental income that assessee entered into L & L agreement in the previous year 2007-2008 with Spanco Telesystems and Solutions Ltd. for giving 4 floors namely 5th, 6th, 7th and 13th floor on leave and license in Infotech Park at Vashi, Navi Mumbai and brought to our notice at page 60 to 98 of the paper book. In April 2008, Spanco Telesystems and Solutions Ltd. informed the Assessee of the slump sale of their unit to Spanco BPO Services Ltd. and Spanco Respondez BPO Pvt. Ltd. and requested the assessee to substitute the names of these new companies as licensee in the assessee's books of accounts. It was submitted that the licensees stopped paying the rent from F.Y. 2010-11 relevant to A.Y. 2011-12 citing financial problems. The closing balance as on 31st March 2011 on account of rent dues was Rs.15.60 cr. However, on a lot of persuasion the licensees paid Rs. 10.51 cr. in the previous year 2011-12 relevant to A.Y. 2012-13 towards old outstanding leaving still the balance of Rs. 7.09 cr. being outstanding rent for the period prior to A.Y. 2012-13. In spite of the same, the assessee offered rental income

for tax in A.Y. 2011-12, but however due to the aforesaid reasons did not offer rental income for tax in A.Y. 2012-13. The licensees did deduct TDS of Rs. 38.58 lakhs and paid the same to the treasury but did not pay any amount to the assessee. He brought to our notice at page 54 to 58 of the paper book.

11. Ld. AR further submitted that income from house property is taxed under section 22 based on annual letting value which is to be arrived at as per section 23 of the Act. The scheme of taxation of house property is based on notional tax which in case of property actually let out is based on actual rent received for the limited purpose of arriving at notional value on which to levy tax. There is no provision in the taxation of income from house property to claim an unrecoverable amount as bad debt. This is in sharp contrast to computation of business income wherein there is a specific provision to claim bad debts. However, the scheme of taxation of house property provides by virtue of section 25A to tax unrealised rent received subsequently. Section 25A is parimateria to section 41 of the Act which deals with taxation of amount of benefit received which was claimed as deduction in the earlier year. On a harmonious reading of the scheme of house

property taxation with the scheme of determination of business income, it is submitted that provision of section 23 should be strictly construed in a situation where the assessee is unable to receive the rent. The strict construction should be in favour of the assessee as explained hereinabove more so when there is no loss of revenue on account of section 25A of the Act but there will be a loss to the assessee and enrichment by the government if unrealised rent is taxed in the absence of any provision for claiming bad debts subsequently.

12. It is submitted that the assessee did not initiate any legal proceedings against the licensees because the licensees were in possession of the premises which was worth more than Rs. 200 cr. Civil litigation would have taken decades for the assessee and during which period the assessee would have been deprived of the possession of its premises. Civil litigation would have also involved huge litigation and opportunity costs. The assessee also relies upon the submissions made to this effect which are reproduced at pg 203 of the paper book in support of its contention as to why no recovery proceedings were initiated against the licensee. It was under these circumstances that the

assessee agreed with licensees on 20th Nov 2011 to give up all its claim in lieu of possession of the premises.

13. He further submitted that it is well settled legal saying that "physical possession is 9/10th of ownership" and the person in possession is in a far superior position irrespective of the legality of the possession. As per section 6 of the Specific Relief Act, a person cannot be dispossessed without due process of law and under the Indian legal system prevailing as of today, the time period for due process of law runs into decades. Even under the Public Premises Act, the government authorities cannot dispossess the person in possession without due process of law. Reliance is placed on the decision of *State of Haryana & Anr. v. Mohinder Pal & Ors.* reported in (2001) 9 SCC 292. The Hon'ble Supreme Court in the case of *Krishna Ram Mahale* reported in (1989) 4 SCC 131 has also observed that under the Indian legal system a person cannot be dispossessed without due process of law. It is, therefore, submitted that the assessee gave up its right to recover the rent because possession was more worthy than the rent. It is submitted that condition of Rule 4(d) should be examined from a businessman's point of view and it was the

commercial and practical call of the assessee not to initiate any legal proceedings in lieu of recovery of the possession.

14. It was submitted that the security deposit of Rs. 7.94 cr. stated by CIT(A) at page 12 of his order was far less than the amount due from licensees for the period prior to A.Y. 2012-13 as evident from pg 55 of the paper book. It is submitted that the assessee only received reimbursement of electricity during the previous year 2011-12 relevant to A.Y. 2012-13. The CIT(A) stated at pg 13 of his order that the holding company of the licensee has profit of Rs. 54.46 cr. It is submitted that the amount was due from the licensees subsidiary of the holding company and not from the holding company and therefore no amount could have been recovered from the holding company. Reliance is placed on the decision of NCLAT in the case of *Anil Syal* reported in **157 SCL 522/113 taxmann.com 52** wherein the proceedings against the parent company to recover dues of sister concern was held to be illegal. Furthermore, in the year 2012, various creditors had filed winding up petition against the holding company and the said holding company was ordered to be wound up by the Hon'ble High Court. It is further important to

note that there was prosecution launched by the department against the group companies of the licensees for non-deposit of TDS, etc. and referred page 235 and 236 of the paper book. It is submitted that merely because the licensees have deducted TDS to save themselves from penal consequences under the Act and to claim deduction on accrual basis, the income cannot be taxed in the hands of the licensor u/s 23 r/w Explanation thereto and Rule 4 of the IT Rules, more so when it is an undisputed position that the assessee has not received any amount towards rent for the previous year 2011-12 relevant to A.Y. 2012-13. Section 25A itself takes care of the taxability of unrealised rent when received subsequently by taxing the same in the year of receipt. In view of above, it is respectfully submitted that the orders of the lower authorities be quashed and no amount can be taxed under the head Income from House Property. Alternatively, it is submitted that only Rs. 38.58 lakhs being TDS deducted can be construed as received by the assessee and only that amount can be taxed and the credit for TDS deducted of Rs 38.58 lakhs by the licensees be granted to the assessee.

15. With regard to disallowance u/s 14A, Ld. AR submitted that assessee is a partner in a partnership firm and has received share of profit amounting to Rs. 2.43 cr. The assessee did not disallow any amount u/s 14A on the ground that no expenses have been incurred to earn the said income. He further submitted that AO has discussed this issue at pg 3 of his order and after applying Rule 8D(2)(iii) computed 0.5% of average investment and disallowed sum of Rs. 1.47 cr. The CIT(A) has discussed this issue at pg 15, para 6.5 and reduced the disallowance to Rs. 44 lakhs by calculating 56% (exempt income/non-operating income) of administrative expenses amounting to Rs. 78,52,422/-. He further submitted that submissions on why no disallowance is to be made are at pages 47 and 51 of the paper book. Furthermore, no disallowance was made on identical situation in A.Y. 2011-12 as evident from page 102 of the paper book. The submissions to CIT(A) on this issue are at page 204 of the paper book. He further submitted that as evident from page 29 of the paper book there is no employee cost of the assessee. The details of administrative expenses are at page 30 of the paper book and on a perusal of the same none of these expenses can be said to have

been incurred even remotely for the purpose of earning share of profit from the firm. It is submitted that the AO has not given any reason for rejecting the submissions of the assessee on why no disallowance should be made but has merely copy pasted extracts of certain Tribunal decisions which were rendered in different context and has no applicability to the facts of the assessee appellant. It is submitted that the AO ought to have examined the facts of the assessee in proper perspective before applying Rule 8D(2)(iii). He further submitted that major expenses pertains to water charges, stock consumption, purchase of diesel, security charges etc. aggregating to more than Rs.78 lakhs and these expenses on the face itself cannot be said to have been incurred for earning exempt income. It is, therefore, submitted that no disallowance ought to be made on the facts of this case as more particularly set out hereinabove and in the absence of any reasons for rejection of the claim made by the assessee appellant on why no disallowance is required to be made.

16. On the other hand, Ld. DR relied on the orders passed by the revenue authorities.

17. Considered the rival submission and material placed on record. We notice from the record that assessee has not received the rent to the extent of Rs. 3,85,85,341/- and the revenue is not disputing the fact. The assessee gave the property at Vashi, Navi Mumbai consisting of 5th, 6th, 7th and 13th Floor to M/s. Spanco Telesystems and Solutions Ltd, on Leave and License basis. Subsequently, the Spanco Telesystems informed the assessee about the slump sale of their business to M/s. Spanco BPO Services Ltd. and Spanco Respondez BPO Pvt. Ltd. and requested the assessee to substitute the names of these new Companies as licensee in their place w.e.f. 01.04.2008. Due to financial problems in the new companies, they stopped making payment towards rent from F.Y. 2010-11 relevant to A.Y. 2011-12. As on 31.03.2011, the total outstanding dues stood at Rs.15-60 crores. After lot of negotiation and persuasion, the assessee was managed to get Rs.10.51 crores during previous assessment year. It is a fact that assessee could not recover Rs.7.09 crores. Since assessee could not recover the rent for the period under consideration, assessee did not declare the rental income for the A.Y. 2012-13. The 'AO' noticed the non-declaration of income

from these properties, he rejected the claim of the assessee and brought to tax by observing that though the assessee fulfils the first 3 conditions of Rule 4 of IT Rules 1962, but has failed to fulfil the 4th condition i.e. the assessee has neither furnished any documentary evidence for instituting any legal proceedings for recovery of outstanding rent nor proved that institution of legal proceedings would be useless. Considering the fact that assessee has to safeguard its interest and initiating litigation against the big business house that too having financial problem will be fruitless and it will be at huge cost. It is also in the interest of the assessee, if it could recover the rent, it will be beneficial to assessee first. No one leaves any money unrecovered. The reasons disclosed by the assessee to close the dispute amicably and recovering an amount Rs.10.51 crores from the company, which were having financial problem itself as huge task.

18. In our considered view, the situation in the present case amply display that institution of legal proceedings would be useless and 'AO' has failed to understand the situation and failed to appreciate the settlement reached by the assessee. AO also not brought on record whether assessee is likely to receive the rent in

near future rather he accepted the fact that it is irrecoverable. The rental income can be brought to tax only when the assessee has actually received or likely to receive or certainty of receiving in the near future. In the given case, the assessee has no certainty of receipt of any rent and as and when assessee reaches an agreement to settle the dispute, it is equal to satisfying the forth conditions in the Rule 4 of the I. T. Rules, 1962. Therefore, in our considered view, the addition of rent is unjustified. Accordingly, we direct AO to delete the addition. Resultantly, Ground no. 1(i) is **allowed**.

19. With regard to Ground No. 1(ii), Ld. CIT(A) has sustained the addition solely on the ground that licensee has deducted TDS on the unrealised rent. Yes, the licensee has deducted TDS and declared the same in the TDS return. They have complied with the advance tax provisions and did not pay any rent to the assessee and it is fact on the record. This alone cannot be the reason to sustain the rental income. As discussed in the earlier para, it is fact on record that assessee has no certainty of receiving any rent. Therefore, we reject the contention of Ld. CIT(A). However, we notice that assessee has taken the TDS

credit to the extent of Rs.38.58 lakhs. The AO can treat the amount of Rs.38.58 lakhs as the income from head “Income from House Property”.

20. With regard to Ground No. 1(iii), it is fact that the assessee has not received rental income for the previous assessment year and any Security/ Rental deposit available is to be adjusted first for old outstanding and if there is any amount remaining unadjusted, the extra rental advance will be adjusted in the current assessment year outstanding. It is undisputed that the rental advance was adjusted for previous assessment year dues and nothing was available for outstanding rent of current assessment year. Therefore, there is no reason for Ld. CIT(A) to give such direction. Therefore, we are inclined to accept the submission of the assessee. Accordingly, this ground of assessee also **allowed**.

21. With regard to Ground No. 2, we notice that assessee has declared exempt income earned by participating in the partnership firm. The AO invoked rule 8D and disallowed u/s 8D(2)(iii) i.e. 0.5% of the average investment for administrative

expenses. On appeal, Ld. CIT(A) reduced the disallowance of Rs.147.97 lakhs to Rs.78.52 lakhs by calculating the ratio of income earned from partnership firm and total non-operating income. We are partly in agreement with Ld. CIT(A) that sometimes, the determination of disallowance under rule 8D is absurd. We may have to go by practical or depending on the facts of the case. The Ld. CIT(A) has accepted that the common other administrative expenses are Rs.78,52,422/-. Assessee has incurred these other administrative expenses for the whole business and Ld. CIT(A) has missed this point and the other administrative expenses incurred for the remaining activities. We do not agree with him on this aspect. The right way of calculating this share of other administrative expenses are to calculate the portion of exempt income to the total income earned by the assessee. In this case, assessee has earned total income of Rs.71,53,93,800/- and earned exempt income of Rs.243,71,741/-. The ratio of exempt income to total income is Rs.3.41%. Therefore, we direct AO to disallow 3.41% of the other common administrative expenses for the purpose of disallowance u/s 14A of the Act.

21.1. On the other hand, assessee submitted that it has not incurred any expenditure in earning the exempt income, therefore this contentions is dismissed. Accordingly, the ground raised by the assessee in this aspect is **partly allowed**.

22. In the net result, the appeal filed by the assessee is **partly allowed**.

Order pronounced in the open court on 06.11.2020.

<p><i>Sd/-</i> (C. N. Prasad) न्यायिकसदस्य / Judicial Member मुंबई Mumbai; दिनांक Dated : <i>Sr.PS. Dhananjay</i></p>	<p><i>Sd/-</i> (S. Rifaur Rahman) लेखासदस्य / Accountant Member 06.11.2020</p>
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आदेशकीप्रतिलिपिअग्रेषित/Copy of the Order forwarded to :

1. अपीलार्थी/ The Appellant
2. प्रत्यर्थी/ The Respondent
3. आयकरआयुक्त(अपील) / The CIT(A)
4. आयकरआयुक्त/ CIT- concerned
5. विभागीयप्रतिनिधि, आयकरअपीलीयअधिकरण, मुंबई/ DR, ITAT, Mumbai
6. गार्डफाईल / Guard File

आदेशानुसार/ BY ORDER,

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