



2. In this case, there was a delay of 67 days in filing the appeal. The assessee filed condonation petition, stating that the assessee's wife diagnosed with cancer, consequently he has to spend lot of time in attending to her and getting the treatment to his wife and in the process, the assessee could not file the appeal before the time allowed under the Act. The assessee also placed the medical certificate, supporting the treatment undergone by Smt.Tulasi, wife of the assessee. We have heard both the parties and condone the delay.

3. The only issue in this appeal is related to the remuneration paid to the Managing Director. During the course of assessment proceedings, the AO found that the assessee has paid the remuneration of Rs.3,00,00,000/- to Sri Tulasi Ramachandra Prabhu, Managing Director of the assessee company. During the year under consideration the company has no turnover except the interest income and the capital gains. In the immediately preceding assessment year, the AO found that the Managing Director was paid the remuneration of Rs.30,00,000/-. Since there was no business in the assessee company, the AO viewed that the payment of Rs.3.00 crores as remuneration to the Managing Director is excessive but not due to the business expediency. Accordingly the AO viewed that the

expenditure was not wholly and exclusively laid out for the purpose of business, hence, allowed the sum of Rs.30,00,000/- and disallowed the balance amount of Rs.2,70,00,000/- and completed the assessment.

4. Against which the assessee went on appeal before the CIT(A) and submitted that the remuneration was actually paid to the Managing Director towards the services rendered by him. The Ld.A.R further submitted that Sri Tulasi Ramachandra Prabhu, the Managing Director is working with the company for long years and the company could not compensate him earlier. Since there were funds available, recognizing the services rendered by the Managing Director, the assessee company paid the remuneration of Rs. 3.00 crores. The assessee further argued that there is no restriction for payment of remuneration as per Companies Act, thus submitted that the remuneration paid to the Managing Director is reasonable and in accordance with the law. Hence requested to delete the addition. The Ld.CIT(A) observed that the assessee company has sold the property and received the sale consideration. In the earlier years, the remuneration paid was only Rs.30,00,000/-, as against which the assessee has paid the remuneration of Rs.3,00,00,000/-, which is unreasonable. During the year under consideration, the assessee has sold the property for

a sum of Rs.6.30 crores and offered the same as capital gains. The Ld.CIT(A) further observed that the assessee could not establish with cogent evidence to show that the payment was made to the Managing Director on prudent business lines. The Ld.CIT(A) further viewed that the payment made to the Managing Director is excessive and accordingly held that the transaction is a colourable device, since the Managing Director was having losses and set off the losses against the remuneration paid by the company. Accordingly confirmed the addition made by the AO and dismissed the appeal of the assessee.

5. Against which the assessee is in appeal before this Tribunal. During the appeal hearing, the Ld.AR reiterated the arguments made before the CIT(A) and submitted that the payment was genuine and the amount received by the Managing Director was offered as income in his hands. The Ld.AR further submitted that there was no limit as per the Companies Act for payment of remuneration to the Managing Director. Neither the AO nor the CIT(A) arrived at the fair remuneration for the services rendered by the Managing Director. The Ld.AR further submitted that in the instant case, the Managing Director was serving the company for a long time and made lot of efforts to dispose off the property for the better price. Since the

amount was paid to the Managing Director as remuneration and the same was also offered as income in his hands, there is no loss of revenue. The Ld.AR argued that the remuneration paid to the Managing Director is genuine and not a case of colourable device, hence, requested to set aside the order of the Ld.CIT(A) and allow the appeal of the assessee.

6. On the other hand, the Ld.DR argued that though there was no limit prescribed by Companies Act for payment of remuneration, the transaction is a colourable device as appearing in page No.4 of the assessment order, wherein, the Managing Director has paid the taxes of Rs.17,049/- after set off of losses from business. Thus argued that higher remuneration was paid to the Managing Director with an intention to reduce the tax burden in the hands of the assessee company and to reduce the losses in the hands of the Managing Director, thus the same was colourable device, hence, argued that the Ld.CIT(A) has rightly restricted the disallowance and no interference is called for.

7. We have heard both the parties and perused the material placed on record. In this case, the company has paid the remuneration of Rs.3,00,00,000/- which the AO viewed that the remuneration paid was excessive compared to the turnover of the company. According to the AO,

there was no turnover in the year under consideration, hence, held that there is no justification for payment of remuneration of Rs.3.00 crores and arrived at the remuneration of Rs.30,00,000/- as reasonable and disallowed the remaining amount of Rs.2,70,00,000/-. The AO did not arrive at the fair and reasonable remuneration payable to the Managing Director and he did not give any basis to disallow the remuneration. According to the Ld.AR the Managing Director travelled extensively and used his influence to identify the buyer to sell the property for higher amount. Apart from the above, the Ld.A.R also submitted that turnover is not only the basis for fixing the remuneration and what is to be considered is the services rendered by the Managing Director to the company. We agree with the contention of the Ld.AR that turnover only cannot be taken as basis for remuneration and it is necessary to look into the services rendered by the M.D. In the A.Y.2014-15, no remuneration was paid to the M.D and in the earlier year also, the remuneration paid to the Managing Director was less and according to the Ld.AR, it does not commensurate with the services rendered by the Managing Director. No outside members are involved in the company except the family members of the Managing Director. It is observed that the Managing Director has offered the income in his hands and paid the taxes thereon. Merely because losses were set off

against the income, it cannot be concluded that the payment of remuneration is a colorable device. Incorrect allowance of loss also is having potential tax effect, thus the reducing the loss is permitted as per law and the same cannot be equated with colourable device. Since the company felt that remuneration paid to the Managing Director was reasonable, burden shifts on the revenue to make out a case of fair value of remuneration with reference to identical facts and comparable cases apropos to the services rendered by the Managing Director. No such exercise was made by the AO. Therefore, we hold that the Ld. CIT(A) erred in upholding the decision of the AO in confirming the addition, hence, we set aside the order of the Ld.CIT(A) and delete the addition made by the AO.

7.1. In addition to the above, as observed from the order of the AO, the case was selected for scrutiny for limited purpose of verifying whether the deduction claimed on account of business loss is admissible or not. The AO did not make any discussion on the deductibility or otherwise of losses and examined the reasonableness of remuneration paid to the Managing Director which is beyond the jurisdiction of the AO as per the scrutiny guidelines. In case the AO intends to examine the issue, the AO ought to have converted the case into complete scrutiny, after obtaining the

approval from the Pr.CIT or CCIT as applicable. No such approval was obtained by the AO before going into the details of reasonableness of remuneration paid to the Managing Director. Therefore on this issue also assessee's appeal deserves to be allowed.

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

Order pronounced in the open court on 23<sup>rd</sup> November 2020.

Sd/-  
(वी.दुर्गा राव)  
**(V. DURGA RAO)**  
न्यायिक सदस्य/**JUDICIAL MEMBER**  
विशाखापटणम /Visakhapatnam  
दिनांक /Dated : 23.11.2020  
L.Rama, SPS

Sd/-  
(डि.एस. सुन्दर सिंह)  
**(D.S. SUNDER SINGH)**  
लेखा सदस्य/**ACCOUNTANT MEMBER**

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

1. निर्धारिती/ The Assessee-M/s Tulasi Cotton Industries Pvt. Ltd., Raj Kamal Complex, Lakshmipuram Main Road, Ashok Nagar, Guntur
2. राजस्व/The Revenue -Asst.Commissioner of Income Tax, Circle-2(1), Guntur
3. The Pr.Commissioner of Income Tax, Guntur
4. The Commissioner of Income Tax (Appeals)-1, Guntur
5. विभागीयप्रतिनिधि, आयकर अपीलीय अधिकरण, विशाखापटणम/DR, ITAT, Visakhapatnam
- 6.गार्ड फ़ाईल / Guard file

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आदेशानुसार / BY ORDER

Sr. Private Secretary  
ITAT, Visakhapatnam