

IN THE INCOME TAX APPELLATE TRIBUNAL  
MUMBAI BENCH "A", MUMBAI  
BEFORE SHRI AMIT SHUKLA, JUDICIAL MEMBER AND  
SHRI GAGAN GOYAL, ACCOUNTANT MEMBER

ITA No. 7814/Mum/2019 (A.Y. 2015-16)

ITA No. 1005/Mum/2021 (A.Y. 2015-16)

Alia Premedia Services Pvt. Ltd.  
1<sup>st</sup> Floor, Om Sadan, Mehra Estate,  
LBS Marg, Vikhroli (West),  
Mumbai-400079

**PAN: AALCA3436C**

..... Appellant

Vs.

Dy. CIT-14(1)(1),  
Aayakar Bhavan, M.K. Road,  
Mumbai-400020.

..... Respondent

Appellant by : Sh. Bhaumik Goda  
Respondent by : Sh. Mehul Jain, Sr.DR  
Date of hearing : 30/05/2022  
Date of pronouncement : 26/08/2022

**ORDER**

**PER GAGAN GOYAL, A.M:**

These two appeals by the assessee are directed against the common order of Ld. Commissioner of Income Tax (Appeals)-22, Mumbai [hereinafter referred to as 'the CIT (A)'] dated 23.08.2019 for the Assessment Years (AY) 2015-16. In ITA No. 7814/Mum/2019, the assessee has raised the following grounds of appeal:

*“1.1. On the facts and circumstances of case, and in law the, the Ld. CIT(A) erred in upholding the order of the DCIT-14(1)(1), Mumbai (“AO”) disallowing the retention bonus amounting to Rs. 1,58,00,000 paid to the Managing Director, Mr. Sethunath Padmanabhan, of the Appellant Company under section 143 sub section 3 r w s 147 of income tax Act which is passed against the principal of natural justice. **[Tax effect relating to each ground of appeal (Rs. 51, 26,310/-).***

*1.2. The Ld. CIT (A) further erred in arriving at his findings and conclusions based on incorrect facts collated from internet search and/or misinterpretation of relevant facts.”*

2. In ITA No. 1005/Mum/201, the assessee has raised the following grounds of appeal:

1. The learned Commissioner of Income Tax (Appeals) erred in upholding the disallowance of Rs 1, 58, 00,000 under section 36(1)(ii) treating the payment of bonus to be excessive and capital in nature.

2. The learned Commissioner of Income Tax (Appeals) erred in treating bonus paid to managing director for services rendered with dividend for the purpose of section 36(1)(ii)

3. The learned Commissioner of Income Tax (Appeals) erred in making disallowance without considering commercial expediency and reasons which lead to payment of bonus

4. The learned Commissioner of Income Tax (Appeals) erred in reaching to its conclusion based on surmises and conjectures without providing assessee an opportunity to presents true facts and thereby violating principles of natural justice.

5. Without prejudice to above, bonus paid by the assessee be allowed under section 37 if it is not admissible under specific section 36(1)(ii) of the Income-tax Act, 1961.

6. The learned Commissioner of Income Tax (Appeals) erred in referring back to the Assessing Officer the issue of credit of TDS appearing in the Form 26AS of ACCPL (the amalgamating company) for verification whether the income also has been accounted for, thereby disregarding and ignoring the detailed written submission dated 1" November 2017, submitted during the course of the assessment.”

3. The facts of the case are that assessee filed its return of income at a loss of Rs 4, 21, 47,185/-. The case of the assessee was selected for complete scrutiny under CASS and accordingly notice u/s 143(2) was issued and duly served upon the assessee.

4. The assessee company is principally engaged in the business of artwork management, reprographics, creative services, digital imaging, prototyping, print management service and pre media services.

5. The assessee company was incorporated in India on 13-02-2013 under the provisions of Companies Act 1956. Pursuant to the scheme of arrangement between Alia Creative Consultant Pvt. Ltd (ACCPL) and the assessee u/s 391 to 394 r.w.s. 78, 100 to 103 of the Companies Act 1956 approved by the Hon'ble High court (Bombay) on 28-02-2014 and filed with office of ROC on 14-03-2014, the company has taken over the cyber back office division and branding division of ACCPL, carrying on business of advertising and publicity agent through different types of mass media w.e.f. 14-03-2014.

6. In consideration as per the scheme of arrangement the shareholders of the AACPL shall receive one fully paid equity shares of Rs 10/- each of the assessee for every 10 equity shares of Rs 10/- each ACCPL they held. Pursuant to the above the company had allotted 1, 02,518 equity share of Rs 10/- each fully paid up on 25-03-2014.

<b>Particulars</b>	<b>Cyber Back Office Division (Rupees)</b>	<b>Alia Branding Division (Rupees)</b>	<b>Total (Rupees)</b>
Gross block	9,683,246	22,919,594	32,602,840
Accumulated	7,105,645	12,746,094	19,851,739

depreciation			
Net block	2,577,601	10,173,500	12,751,101
Trade receivables	8,291,172	20,475,195	28,766,367
Cash a bank	539,495	1,579,977	2,119,472
Short term loans and advances	302,700	1,857,246	2,159,946
Total assets(A)	11,710,968	30,085,918	45,796,886
Trade payables	400833	1,563,115	1,963,948
Other current liabilities	193,976	5,147,172	5,341,148
Total Liabilities (B)	594,809	6,710,287	7,305,096
<b>Surplus (A-B)</b>	<b>11,116,159</b>	<b>27,375,631</b>	<b>38,491,790</b>

7. As per the accounting treatment prescribed in the scheme of arrangement the company shall record all the asset and liability of Cyber Back Office Division and Alia Branding Division at the respective book values as appearing in the books of ACCPL as on the appointed date. As a result , the value of Cyber Back Office Division of Rs 11,116,159/- and Alia Branding Division of Rs 27,375,980/- has been transferred to the company and adjusted against the face value of 102,518 equity shares of Rs.10/- each fully paid up. The difference of Rs 37,466,959/- has been transferred to capital reserve account.

8. As the case was selected under the category of complete scrutiny, and there is no allegation emanating from the order of AO and Id CIT (A) about any sort of non-cooperation or non furnishing of any information/document required hence it can be reasonably presume that the books of accounts of the assessee

and transactions entered into are broadly bonafide. There may be a difference of opinion in terms of allow ability /disallow ability of any particular expenditure or of revenue but the presentation of accounts are not under doubt.

9. This fact has been further substantiated by the Id. CIT (A) in her/his order vides pg no 13 Para 3.3(2), reproduced as under:

*“The financial statements of the Company have been prepared in accordance with generally accepted accounting principles in India (Indian GAAP). The Company has prepared these financial statements to comply in all material respects with the accounting standards specified under Section 133 of the Act, read with Rule 7 of the Companies (Accounts) Rules, 2014 and the relevant provisions of the Companies Act, 2013. The financial statements have been prepared under the historical cost convention on an accrual basis except in case of assets for which provision for impairment is made. The accounting policies have been consistently applied by the Company and are consistent with those used in the previous year.”*

10. During the course of assessment proceedings it was noticed that the assessee has paid a bonus of Rs 1.75/-cr to its managing director Mr Sethu Nath Padmanavhan Kutty (SPK). It is also noticed that Mr SPK is also a share holder of 7% shares in the assessee company, in the view of these facts; A.O issued a show cause as to why bonus paid to Mr SPK should not be disallowed u/s 36(1) (ii) of the I.T. Act 1961.

11. In response to this show cause assessee filed various data of sales, net profit and increase in clientele base. In addition to these financial submissions assessee also filed various pronouncements of apex court, various high courts and ITAT in its favour. The A.O was not satisfied with the response of the assessee and case laws relied upon in its favour.

12. In the result of above assessing officer made an addition of Rs 1.58/- Cr. u/s. 36(1) (ii). Against this action of A.O assessee preferred an appeal before the office of Id. CIT (A) (22), Mumbai. Before the Id. CIT (A) assessee argued its matter in detail by filing various documents and case laws in its favour. Here also assessee was not able to succeed hence this appeal is preferred before us. We have gone through the order of the A.O, order of the Id. CIT (A), submissions of the assessee before the A.O and Id. CIT (A). In addition to this we have gone through and consider the factual paper-book dated 18-04-2022, and 09-06-2022 and the legal paper-book filed before us.

13. For a proper appreciation of the matter we are reproducing certain relevant portions of the order of Id. CIT (A) as here-in-below.

**“It also appears from the internet search about Alia Premedia Services Pvt Ltd that this brand advertising division of the company was sold off and/or demerged from the company during next two assessment years i.e. AY 2016-17 and AY 201718 and the assessee was engaged in the business of exporting paper for the year ended 31.03.2018 and Mr. SPK moved over to new company as a director/employee on revised terms and conditions.**

Thus it becomes clear from the foregoing details that the services of SPK were mainly hired not for promoting the nature of business of 'brand building' in India but actually to demerge the old business of the erstwhile company into that of the assessee, issue of Share capital to Vavinel SAS and Diadeis Maurice Ltee and carry out relevant transactions during the year and that was the main purpose of the assessee company in hiring the services of SPK. Moreover, the remuneration package of RPK increased from Rs.39,00,000/- for AY 2014-15 to Rs.2,36,10,000/-

for AY 2015-16 whereas turnover had increased twofold only. However, the profits for AY 2014-15 of Rs.53, 55,733/- were converted into a whopping loss of Rs.5, 01, 08,075/-. It also appears from the records that 'there was threefold increase in employee remuneration and fourfold increase in professional fees from Rs.42,87,390/- to Rs.1,76,36,468/- during the year as compare to last AY 2014-15, it is also probable and possible that the expenses of the erstwhile company ACCPL with whom the company entered into services arrangements agreements were also debited to the accounts of the company and major part of other expenses, including bonus payments to SPK were incurred towards negotiating merger of business and companies and issuing share capital to foreign parties and negotiating and following up with all the authorities in this regard from time to time. Even then the benefit of these mergers and demerger of businesses did not result in any Net Business Profit to the assessee as is clear from the following chart:

<b>NAME OF THE CLIENT</b>	<b>AY 2014-15</b>	<b>AY 2015-16</b>	<b>AY 2016-17</b>	<b>AY 2017-18</b>
Cadbury (Mondelez)	13,60,517	1,48,50,241	1,76,65,791	1,75,79,972
Unilever Group	18,17,255	86,83,450	1,28,96,062	1,26,46,775
<b>Total</b>	<b>96,28,005</b>	<b>10,35,32,442</b>	<b>12,99,69,811</b>	<b>16,08,50,134</b>

The turnover and Net profit for the year under consideration and the subsequent years have been summarized as under:

<b>Particulars</b>	<b>AY 2014-15</b>	<b>AY 2015-16</b>	<b>AY 2016-17</b>	<b>AY 2017-18</b>
Revenue from operations	47,70,11,257	14,37,33,618	18,82,33,040	24,23,56,266

Net Profit before tax	29,51,894	-5,54,29,503	1,03,10,094	4,07,32,464
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Ultimately the assessee ended up incurring a net loss of Rs.0.15 lakhs (5.541.04.4.07-0.29) upto AY 2017-18 and everything evened out and the business of brand building was transferred to a new company Diadeis and Vavinel, SPK left the assessee company and joined a new company of the Deidias Group and the assessee company went on to start new business activity of exporting paper from AY 2018-19 onwards. Therefore, the assessee company did not gain much from this entire exercise except acting as an intermediary to circumvent some rules and regulations for acquiring the business of ACCPL and ultimate transfer of the brand building business to a new company owned by the Diadeis and Vavinel. Thus circle is complete whereby the funds moves from the brand advertisers to associated parties and spending it lavishly to achieve the main purpose of transfer of business from ACCPL to itself and ultimate transfer to a new company and carrying out the main purpose of mergers and demergers of businesses to benefit the foreign shareholders and it is possible that all these expenses which appear to be capital in nature and which should have been incurred by the foreign parties were incurred by the assessee and camouflaged as business expenses of the assessee. Moreover it is worth noting here that the annexure A to the agreement dated 22.07.2014 with SPK does not mention anything about payment of bonus to him and thus the payment of bonus of Rs.1,75,00,000/- was beyond the clauses of the terms and conditions of the agreement and yet the AO has allowed a deduction for Rs.17,00,000/- out of Rs.1,75,00,000/- in addition to other remuneration of Rs.61,10,000/-

(2,36,10,000/ -- 1,75,00,000). Thus it is held that the payment of bonus of Rs. 1,58,00,000/- the appellant SPK was not only excessive vis-a-vis the business needs of the assessee but was also capital in nature in light of the facts narrated in the foregoing paragraphs and therefore the disallowance of bonus of Rs. 1,58,00,000/- u/s.36(1)(ii) made by the AO is upheld in facts of the assessee's appeal in respect of ground of appeal No. 1 is dismissed.”

14. From the facts mentioned above including the order of AO and relevant extracts reproduced supra from the order of Id. CIT (A), it emanates that both the authorities relied upon different logics and facts to arrive at their respective decisions. Both the decisions are in contradiction to each other, i.e., AO relied on disallowance of sec 36(1) (ii) based on the fact that the employee MD is a share holder also of 7% equity share. Hence he applied section 36(1) (ii). Whereas Id. CIT (A) confirms the AOs order not on the facts relied upon by the AO but he extrapolated his own theory of facts as enumerated (supra) vide pg no 19, 20 and 21 of Id. CIT (A) order.

15. About the validity of the findings based on facts by both the authorities we will discuss later on in this order. But, one thing is sure the findings of Id. CIT (A) is not at all relevant for the purposes of sec 36(1) (ii) of the act. His findings may be relevant in the context of sec 37 of the act but not in the context of sec 36(1) (ii) of the act. His confirming the order of AO i.e. disallowance made u/s 36(1)(ii) of the act, but to confirm the same instead of focusing and applying the conditions prescribed u/s 36(1)(ii) of the act rather he is pitching for the conditions applicable to sec 37 of the Act.

16. As per the “Doctrine of merger” once an order u/s 250 of the Act passed by the CIT (A) order of the AO gets merged into that order. In this case the grounds on which AO made disallowance u/s 36(1) (ii) of the Act along with submissions of the assessee nowhere considered by the Id CIT (A). In that situation it can be reasonably held that Id. CIT (A) was agreed with the submissions of the assessee and brushed aside the findings of the AO. To justify the action of AO/to rectify the order of AO he rather pitched and applied the conditions relevant to sec 37[although he also disallowed the same u/s 36(1) (ii)]. With the discussions of the facts and law mentioned supra it can be held that the action of Id. CIT (A) tantamount to enhancement of income in substance and confirmation of AOs order in form. We don’t hesitate in applying here the concept of substance over form. With these discussions of substance over form, we observed as emanates from the record that no notice of enhancement u/s 251 of the Act had been issued hence the action of Id. CIT (A) is bad in law as it defeats the principle of natural justice and lack of jurisdiction.

17. Nevertheless, now we will analyze the action of AO and Id. CIT (A) based on their respective findings.

18. We are reproducing herein below the relevant extract of the AOs order as per Para 4.5 and 4.6 on pg 6 and 7 of AOs order.

*“In view of the discussion held in foregoing paras. It is held that the excessive amount of bonus is paid to Mr. Sethunath Padnanabhan, Managing Director of the assessee company mainly because he is a shareholder in the company. However, considering that he has rendered services also, a sum of Rs. 17 lakhs (taking the comparable of bonus paid of Rs. 16,99,987/- to Mr.Hemant Jain) is treated as the reasonable bonus and the balance of Rs.58.00,000/- (1,75,00,000 - 17,00,000) represents the sum that would have been payable to him as profit or dividend if it*

*had not been paid as bonus or commission and thus disallowable under section 36(1)(ii) of the Act.*

*Further, this argument also of the assessee that there is no tax avoidance as Mr. Sethunath Padnanabhan too falls under 30% tax bracket is not correct. If Mr. Sethunath Padnanabhan is offering the income at tax rate of 30% the assessee company is getting deduction at 30% and in addition to that by not paying this sum as dividend to the shareholder (Mr. Sethunath Padnanabhan in this case) the assessee company is avoiding the dividend distribution tax @ 15%. Thus, it is evident that there is the tax avoidance by entering into this transaction."*

19. Considering the order of the AO, submission of the assessee and financial facts of the assessee, it can be reasonably observed as under:

*i) The bonus paid to Mr. SPK was of contractual nature. In the agreement between the assessee and Mr. SPK, board of the Company was empowered to determine the amount of retention bonus as the same can be observed vide pg -33 of the factual paper-book filed on 18-04-2022.*

*ii) Mr. SPK was the shareholder for 7% only in that circumstance even if assuming the whole amount available to the company available for distribution of dividend, share of Mr. SPK will be in negative as Company have reported a loss of Rs 3, 79, 39,503/- even without considering the retention bonus paid to Mr. SPK and hence there is no question of dividend payout.*

*iii) The appellant Company in absence of profit for the year as also having sufficient accumulated free reserves and a dividend history was not eligible to declare dividend as per the proviso to sec 123 of the Companies Act 2013 r.w. rule-3 of Companies Rule 2014.*

*iv) Bonus in the guise of dividend usually being planned for majority shareholder, here Mr. SPK was holding only 7% and that is to after serving the assessee almost for 3 years as per retention bonus terms he left the company and joined somewhere else. So it clearly shows that for a person having 7% equity and 3 years of term no such planning can be thought of even.*

*v) In the relevant assessment year even after excluding the amount of retention bonus paid Company was at loss of around Rs 3,79,39,503/-, whereas Mr. SPK was already in the slab of 30% whereas there was no tax benefit to the assessee in the relevant assessment year. As far as the loss of DDT as assumed by*

*the AO in the given set of facts is full of over thinking hence, simply a conjunction surmises and guesswork.*

20. Our observation based on relevant extract reproduced of Id. CIT (A) as under:

***i) Finding/allegation of Id. CIT (A).***

*It also appears from the internet search about Alia Premedia Services Pvt. Ltd that this brand advertising division of the company was sold off and/or demerged from the company during next two assessment years i.e. AY 2016-17 and AY 2017-18 and the assessee was engaged in the business of exporting paper for the year ended 31.03.2018 and Mr. SPK moved over to new company as a director/employee on revised terms and conditions (Page 19 of CIT(A) order)*

**Our Observation**

- . Branding division was not sold off/demerged by Appellant in AY 201617 or AY 2017-18.
- . Even today, Appellant is engaged in the said business.
- . Refer financial statement for AY 201617, AY 2017-18 which demonstrates that business is not sold or demerged. This fact can be seen from Revenue Schedule at Note 19 of AY 2016-17, AY 2017-18. [Page 24 and 54 of supplemental factual paper book]

***ii Finding/allegation of Id CIT (A).***

*Services of SPK were mainly hired not for promoting the nature of business of 'brand building' in India but actually to demerge the old business of the erstwhile company into that of the assessee, issue of share capital to Vavinel SAS and Diadeis Maurice Ltee and carry out relevant transactions during the year and that was the main purpose of the assessee company in hiring the services of SPK (Page 19 of CIT (A) order)*

## **Our Observation**

- . SPK was managing director of the Appellant and was responsible for performance of Appellant.
- . Branding division was demerged into Appellant Company in AY 2014-15 (i.e. year prior to year under consideration). Appointed date of demerger was 1 October 2013 [Refer High Court order approving demerger scheme] [Page 94-114 of supplemental factual paper book]
- . As consideration of demerger shares were issued to shareholder of demerged Company in AY 2014-15.
- . Subsequently, in AY 2015-16 Vavinel SAS acquired 74% from Mr. Sanjeev and Mrs. Aneeta Malhotra. This is secondary sale between shareholders which does not involve any issuance of shares by appellant.
- . Ld. CIT (A) observation that Alia Premedia issued shares to Vavinel SAS is incorrect. In AY 2015-16 there was no issuance of shares.
- . Change in shareholder as secondary sale is evident from Note 4(d) of AY 2015-16 (FY 2014-15) financial statement as also comparative shareholding extracted by CIT (A) at Page 14 of CIT (A) order. [Refer Note 4 at Page 65 of factual paper book]

### ***iii. Finding/allegation of Id. CIT (A).***

*It also appears from the records that 'there was threefold increase in employee remuneration and fourfold increase in professional fees from Rs.42,87,390/- to Rs.1,76,36,468/- during the year as compare to last AY 2014-15, . It is also probable and possible that the expenses of the erstwhile company ACCPL with*

*whom the company entered into services arrangements agreements were also debited to the accounts of the company and major part of other expenses, including bonus payments to SPK were incurred towards negotiating merger of business and companies and issuing share capital to foreign parties and negotiating and following up with all the authorities in this regard from time to time (Page 19 and 20 of CIT(A) order).*

## **Our Observation**

. Books of account of Appellant are audited by auditors and hence it is not possible to debit expenditure of any other company. This point is not also raised by learned AO. Allegation of Hon'ble CIT (A) is not substantiated by facts.

- There is no merger of business in AY 2015-16 or even in subsequent years till date.

- Further, as stated above in Sr No 3, there is no issuance of shares to foreign parties.

### **iv. Finding/allegation of Id. CIT (A).**

*Ultimately the assessee ended up incurring a net loss of Rs.0.15 lakhs (5.54-1.04.4.070.29) up to AY 2017-18 and everything evened out and the business of brand building was transferred to a new company Diadeis and Vavinel, SPK left the assessee company and joined a new company of the Deidias Group and the assessee company went on to start new business activity of exporting paper from AY 2018-19 onwards. Therefore, the assessee company did not gain much from this entire exercise except acting as an intermediary to circumvent some rules and regulations for acquiring the business of ACCPL and ultimate transfer of the brand building business to a new company owned by the Diadeis and Vavinel. Thus circle is complete whereby the funds moves from the brand advertisers to associated parties and spending it lavishly to achieve the main purpose of transfer of business from ACCPL to itself and ultimate transfer to a new company and carrying out the main purpose of mergers and demergers of businesses to benefit the foreign shareholders and it is possible that all these expenses which appear to be capital in nature and which should have been incurred by the foreign parties were incurred*

*by the assessee and camouflaged as business expenses of the assessee. (Page 20 of CIT (A) order)*

### **Our Observation**

. Brand division is not transferred to any company. As stated above, even today Appellant continues to engage in the said business.

. Exporting paper was one of the businesses of the company which was pursued along with brand business division. This fact can be seen from Revenue Schedule at Note 19 of AY 2018-19. [Page 93 of supplemental factual paper book]

. Allegation of transfer of funds from brand advertisers to associated parties is baseless and without any evidence. Appellant strongly refuses the same.

21. Considering the above facts discussed emanated out of the orders of the authorities below and submission of the assessee order of Id. CIT (A) is not sustainable as the same is bad in law.

**22. In the result both the appeals of the assessee are allowed.**

Order pronounced in the open court on 26<sup>th</sup> day of August, 2022.

Sd/-

(AMIT SHUKLA)  
JUDICIAL MEMBER

Sd/-

(GAGAN GOYAL)  
ACCOUNTANT MEMBER

Mumbai, दिनांक / Dated: 26/08/2022

SK, Sr.PS

**Copy of the Order forwarded to:**

1. अपीलार्थी / The Appellant ,
2. प्रतिवादी / The Respondent.
3. आयकर आयुक्त (अ) / The CIT(A)-
4. आयकर आयुक्त CIT
5. विभागीय प्रतिनिधि, आय.अपी.अधि., मुंबई / DR, ITAT, Mumbai

6. गार्ड फाइल / Guard file.

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BY ORDER,

(Dy. /Asstt. Registrar)  
**ITAT, Mumbai**