

IN THE INCOME TAX APPELLATE TRIBUNAL  
MUMBAI BENCH "B", MUMBAI

BEFORE SHRI MAHAVIR SINGH, JUDICIAL MEMBER  
AND SHRI RAJESH KUMAR, ACCOUNTANT MEMBER

ITA No. 2716/MUM/2011  
(Assessment Year : 2007-08)

Birla Sunlife Asset Management Co. Ltd.  
One Inida Bulls Centre,  
17<sup>th</sup> Floor, Jupiter Mill Compound,  
841, Senapati Bapat Marg,  
Elphinstone Road, Mumbai 400013  
PAN: AAACB 6134D ... Appellant

Vs.

The Addl. CIT, Range 8(1),  
Aaykar Bhavan, MK Road,  
Mumbai 400 020 .... Respondent

ITA No. 2698/MUM/2011  
(Assessment Year : 2007-08)

The DCIT, Range 8(1),  
Aaykar Bhavan, MK Road,  
Mumbai 400 020 ... Appellant

Vs.

Birla Sunlife Asset Management Co. Ltd.  
One Inida Bulls Centre,  
17<sup>th</sup> Floor, Jupiter Mill Compound,  
841, Senapati Bapat Marg,  
Elphinstone Road, Mumbai 400013 ... Respondent

Revenue by : Shri Premand J.  
Assessee by : Shri Yogesh A. Thar

Date of hearing : 10/05/2016  
Date of pronouncement : 18/05/2016

**ORDER****PER MAHAVIR SINGH, J.M:**

These cross appeals are arising out of order of CIT(A)-16, Mumbai in Appeal No.CIT(A)-16/IT-410/2009-10 order dated 12/01/2011. Assessment was framed by the Addl. CIT, Range8(1), Mumbai under section 143(3) of the Income Tax Act, 1961 (hereinafter referred as 'the Act') vide his order dated 30/12/2009 for the assessment year 2007-08.

2. The inter-connected issues raised by both the parties is with regard to the order of CIT(A) partly allowing the claim of expenses i.e. compensation on account of redemption of units and also claim arising out of embezzlement. For this assessee has raised the issue regarding disallowance of compensation paid to investors of Rs.50,86,434/- by the following three grounds:

*(i) On the facts and in the circumstances of the case and in law, the learned Commissioner of Income Tax(Appeals) (hereinafter referred as CIT(A)) erred in confirming the action of Additional Commissioner of Income Tax (hereinafter referred as Assessing Officer) of disallowing compensation paid to investors of Rs.50,86,434/- in the course of business.*

*ii. The learned CIT(A) & Assessing Officer failed to appreciate and ought to have held that:*

➤ *The compensation paid to investors as per the statutory regulation of SEBI and Mutual Fund guidelines prescribed by them, which has to be borne by asset Management Company.*

➤ *The Appellant's claim that compensation paid to investors are business loss and allowable under section. 37 of the Income Tax Act;*

*(iii)The Appellant prays the disallowance of compensation paid to investors of Rs.50,86,434/- be allowed as deduction under section.37(1).*

Revenue has raised the following ground against the order of CIT(A) deleting disallowance claimed by the assessee on account of embezzlement:-

*"1. On the facts and circumstances of the case and in law, the Ld. CIT(A) erred in deleting the disallowance made by the AO of Rs.50,57,940/- being deduction claimed by the assessee in respect of interest on the embezzled amount, without appreciating the facts of the case."*

3. Briefly stated, the facts are that assessee company is engaged in the business of asset management, portfolio management and advisory services. The assessee filed complete books of accounts and audited accounts during the course of assessment proceedings. The Assessing Officer noticed from the return of income that the assessee has claimed the following expenses in its profit and loss account and the details are given in the assessment order para -4 as under:-

Investor Name	Date	Amount	Description
Ramadevi Sood	5/3/2006	1598083	Units erroneously not allotted to the investor in Jan. 2000
Turquioiuse Ltd.	7/5/2006	5057940	Redemption of units on forged redemption request
V. Meenakshi	7/13/2006	696257	Non receipt of dividend warrant
V. Meenakshi	8/22/2006	654959	Interest on delayed dividend payment
Naresh Kumar Trehas	3/31/2007	883000	Compensation to investor for redemption proceeds
Various Investors		1254135	Compensation expenses various investors of amount below Rs.5 Lacs

Total		10144374	
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The Assessing Officer noted that the claim of embezzlement amounting to Rs.3,92,15,599/- was disallowed by the Assessing Officer in assessment year 2004-05, which was upheld by CIT(A) as well as ITAT. He noted that the assessee being Asset Management Company for Birla Sunlife Mutual Fund, was asked to submit agreement between the Registrar and the Transfer Agent and the assessee company. The assessee appointed the Citi Bank as Registrar and the Transfer Agent. According to Assessing Officer the Registrar and Transfer Agent was directly responsible on redemption made from the mutual fund but the assessee's choice to pay investor by making the investor to subrogate all and any rights/interest, title in respect of any proceeds recovered or recoverable from any other source including from the fraudster on account of units unauthorizedly redeemed from the family members. According to Assessing Officer the amount paid to the unit holders is not liability of the assessee and hence he disallowed the claim made in respect to the amount of Rs.50,57,940/- in respect to Torquoise Investments Finance Private Limited('TIFPL') For redemption of units of forged redemption requested for the balance sum of Rs.50,86,434/-, the Assessing Officer noted that the assessee is only a fund manager of Birla Mutual Fund and, if any, unit is not allotted to any investor, that cannot be the liability of the assessee and, therefore, he disallowed the claim of compensation in respect to Smt. Ramadevi Sood amounting to Rs.15,98,083/-, Smt. V. Meenakshi amounting to Rs.6,96,257/-, Smt. V. Meenakshi amounting to Rs.6,54,959/- and Naresh Kumar Trehas

amounting to Rs.8,83,000/- and authorized other small investors mounting to Rs.12,54,135/-. Aggrieved, assessee preferred appeal before CIT(A) against the disallowance.

4. The CIT(A) after considering the submissions of the assessee in respect to payments made to certain investors aggregating to Rs.50.86 lacs, pertaining to legacy of the earlier period, the CIT(A) noted that this amount is in the nature of compensation and the claim was verified and approved for payments. According to him, this is evident from the statement documenting the management decision, a copy of which is furnished before him but CIT(A) was of the view that once the account is settled with the mutual fund after taking into consideration the deficit and surplus existing in the accounts of the Registrar and Transfer Agent i.e Karvy Consultants the entire responsibility of taking care of the liability arising or accruing thereafter rests with the mutual fund and not with the assessee. Accordingly he confirmed the action of the Assessing Officer by observing as under:- (only relevant portion of para 3.3.1)

*"..... I find that there is no merit in the argument of the appellant. Once, the account is settled with the mutual fund after taking into consideration the deficit and surplus existing in the account of the registration and transfer agent viz. Karvy Consultant, the entire responsibility of taking care of any liability arising or accruing thereafter rests with the mutual fund and not with the appellant. Therefore, the liability to compensate or to make payment to the parties in question rests with the mutual fund and not with the appellant. Therefore, I am in agreement with finding of the Ld. A.O that the amount in question is not the liability of the appellant. Further, I also find that there is no material placed either before the Ld. A.O or before me to prove the factum of the transaction. In view of this, the addition made by the Ld. A.O is confirmed and this ground of appeal is dismissed."*

Aggrieved against action of CIT(A) confirming the order of the Assessing Officer, assessee preferred second appeal before the Tribunal.

5. Before us, Ld. Counsel for the assessee argued that the assessee is an Assessment Management Company of Birla Sunlife Mutual Fund Ltd. and as mutual fund regulations issued by SEBI for carrying out mutual fund business a Trust is required to be created with the Board of Trustees and the unit holders. The unit holders are beneficial owners of the Trust. The Trustees of the Trust appoint the Asset Management Company, the assessee, for carrying day to day activities like fund raising from investors, issuance of unit to investors, management of funds, issuing and accounting of redemption proceeds, issuing and accounting dividend warrants, etc. He explained that the asset Management Company does necessary activity for the beneficial owners and for the same charging asset management fee from the various schemes as per SEBI regulations. In this process the assessee company has settled claim towards compensation to various investors on account of business expediency and as per regulations of SEBI amounting to Rs.50,86,431/- (the details are given above, which are reproduced from the assessment order). The assessee has claimed these expenses as deduction, which was incurred, according to the Ld. Counsel for the assessee in the course of business on account of business expediency. The Ld. Counsel for the assessee explained that the assessee has to incur such expenses to safeguard its business interest against complaint made by investors on SEBI, which may lead to violation of SEBI regulations and also it is duty bound to make the

loss good of the investors. He explained that the assessee and Trustees of the mutual fund entered into an investment management agreement, which was guiding factor for rights and obligation of Asset Management Company. Ld. Counsel for the assessee also explained that this issue of reconciliation came up during the assessment year 2002-03, wherein the reconciliation difference amounting to Rs.16.00 crores was deficit against the mutual fund and Rs.6.00 crores being surplus in favour of the mutual fund. But there was a net deficit of Rs.10.00 crores against mutual fund. The assessee appointed a firm of Chartered Accountant to carry out this reconciliation and after prolonged exercise the difference largely remain unrealized and the matter was taken-up with SEBI and in consultation with SEBI it was decided that the deficit of Rs.16.00 crores should be made over by Asset Management Company and replenished to the mutual funds. Ld. Counsel for the assessee explained that out there are unknown credits lying in the bank account to the extent of Rs.6.00 crores was adjusted and balance Rs.10.00 crores were paid to mutual funds. He explained that in assessment year 2002-03 the Tribunal taking note of the provisions of the Act and SEBI Regulations, contractual agreement between assessee and the prospects of mutual fund held that the assessee was contractually and statutorily bound to make the payment so as to keep assessee's business interest and, therefore, held that making good of deficit of Rs.16.00 crores, after adjusting credits of unknown bank balance of Rs.6.00 crores, balance amount of Rs.10.00 crores is allowable as deduction. The entire legacy pertain to earlier period, which was claimed amounting to Rs.50.86 lacs in respect to above noted five

persons. The assessee stated that above payments qualify for allowance for the reason that these are commercial expediency, contractual obligations and statutory obligations. Hence, Ld. Counsel for the assessee requested for allowance of this deduction.

6. On the other hand, the Sr. D.R supported the order of the CIT(A) on this issue and stated that once the accounts are settled with the mutual funds, after taking into consideration the deficit and surplus existing in the accounts of Transfer Agent, the entire responsibility, any liability arising or accruing thereafter, of settlement, rests with the assessee. According to him, this cannot be allowed as deduction and CIT(A) has rightly upheld the same.

7. We have heard the rival contentions on this issue and gone through the facts and circumstances of the case. We find from the facts of the case that the Trustees of the Trust appointed the assessee for carrying day to day activities like fund raising from investors, issuance of unit to investors, management of funds, issuing and accounting of redemption proceeds, issuing and accounting dividend warrants, etc. We find from the facts of the case that that the assessee does necessary activity for the beneficial owners and for the same charging asset management fee from the various schemes as per SEBI regulations. We also find that in this process the assessee company has settled claim towards compensation to various investors on account of business expediency and as per regulations of SEBI amounting to Rs.50,86,431/-. The complete details are given in the assessment order. The assessee

has claimed these expenses as deduction, which was incurred, in the course of business on account of business expediency. As claimed by the assessee, we are of the opinion that in such nature of business, the assessee has to incur such expenses to safeguard its business interest against complaint made by investors on SEBI, which may lead to violation of SEBI regulations and also it is duty bound to make the loss good of the investors. We also find from the facts of the case that the assessee and Trustees of the mutual fund entered into an investment management agreement, which was guiding factor for rights and obligation of Asset Management Company. We also find that the assessee has raised this issue and filed reconciliation during the assessment year 2002-03, wherein the reconciliation difference amounting to Rs.16.00 crores was deficit against the mutual fund and Rs.6.00 crores being surplus in favour of the mutual fund. But there was a net deficit of Rs.10.00 crores against mutual fund. The assessee appointed a firm of Chartered Accountant to carry out this reconciliation and after prolonged exercise the difference largely remain unrealized and the matter was taken-up with SEBI and in consultation with SEBI it was decided that the deficit of Rs.16.00 crores should be made over by Asset Management Company and replenished to the mutual funds. It is also a fact that out there are unknown credits lying in the bank account to the extent of Rs.6.00 crores, which was adjusted and balance Rs.10.00 crores were paid to mutual funds. As explained by the Ld. Counsel for the assessee before us now and he relied on Tribunal decision assessee's own case wherein, in assessment year 2002-03 the Tribunal taking note of the provisions of the Act and

SEBI Regulations, contractual agreement between assessee and the prospects of mutual fund, held that the assessee was contractually and statutorily bound to make the payment so as to keep assessee's business interest and, therefore, held that making good of deficit of Rs.16.00 crores, after adjusting credits of unknown bank balance of Rs.6.00 crores, balance amount of Rs.10.00 crores is allowable as deduction. We find that the assessee is carrying over the entire legacy pertain to earlier period, for which, it claimed amounting to Rs.50.86 lacs in respect to above noted five persons. Now the question arises, whether the above payments qualify for allowance for the reason that these are commercial expediency, contractual obligations and statutory obligations. We are of the view that in the present case the unit holders, who made claim with the transfer agent, are entitled for return of their money invested in assessee's mutual fund. Even the SEBI Regulation states so and if there is violation of the same, SEBI can prosecute the assessee. It means that the liability paid by assessee is in the nature of statutory as well as contractual. The assessee has paid the legitimate claim of the unit holders, who have lodged the claim with the Registrar and Transfer Agent of the issue. We are of the view that this expenditure is incidental to trade itself and Assessing Officer cannot ignore the same. We are of the view that even this comes within the ambit of commercial expediency for the reason that this is indirectly for facilitation of carrying on of the business of the assessee. In view of this reasoning, we allow the claim of the assessee and the orders of the lower authorities on this issue are reversed. This issue of assessee's appeal is allowed.

8. The issue in Revenue's appeal as regards to disallowance of claim of assessee in respect to redemption of units on forced redemption request in the case of TIFPL. Briefly stated, the facts are that TIFPL made an investment on 30/07/2002 by appointing an investment portfolio. There were four transactions of subscriptions and redemptions for all units in its investment account from August 2002 to February, 2003. TIFPL applied for redemption of all outstanding investments as on 28/03/2003 and Rs.4.85 crores being value of outstanding units to the credit of TIFPL were paid on 31/03/2003. TIFPL informed the assessee that total amount expected from final redemption is Rs.7.50 crores as against receipt of Rs.4.85 crores, but assessee informed TIFPL that the balance units of Rs.3.65 crores were already redeemed by it on 28/02/2003. TIFPL informed that they have not redeemed the same and there is some mistake on the part of the assessee. On investigation, it was found that a fraudulent request for redemption was submitted on 28/02/2003 with assessee's Registrar i.e. Turner Morrison Branch, Citi Bank being Registrar and Transfer Agent processed such request and forwarded the same to assessee's Turner Morrison Branch. Accordingly, a redemption cheque of Rs.3.65 crores was handed over to fraudulent person on 03/03/2003. To encash this amount of mutual fund redemption, a fraudulent bank account was opened with IDBI Bank on 7/3/2003 and this redemption cheque of Rs.3.65 crores was deposited in the high value clearing on 10/03/2003 and was cleared on the same day. Qua this FIR was registered on 7/4/2003 in MRA Marg Police Station and a complaint with Banking

Ombudsmen was also filed on 29/09/2003. The assessee during the assessment year 2004-05 made a provision in its books of account amounting to Rs.3,92,15,599/-. The assessee claimed this amount as expenditure during the course of assessment proceedings for the assessment year 2004-05 but Assessing Officer has disallowed the same for the reason that expenditure is not crystallized. The CIT(A) as well as ITAT confirmed the action of the Assessing Officer by stating that the claim of deduction on account of expenditure is premature and not crystallized as yet. During the year under consideration the assessee has made payment of Rs.4,42,73,539/- on 28/07/2006 vide cheque No.112500 as full and final settlement to TIFPL. This payment was against the opening provision made during the financial year 2004-05 relevant to assessment year 2005-06 amounting to Rs.3,92,15,599/-. The assessee also debited the balance amount of Rs.50,57,940/- to the profit and loss account and claimed under the head compensation, which was disallowed by the Assessing Officer. Aggrieved, assessee preferred an appeal before CIT(Appeals) who allowed the claim of the assessee vide para 2.3.1 of his appellate order, which reads as under:-

*"2.3.1 I have carefully considered the contention of the appellant company as well as carefully gone through the available documents on record. I find that the inalienable fact of the appellant's case is that the TIFPL made an investment with the appellant on July 30, 2002. The redemption was due on February 5, 2003. The appellant on receipt of request for redemption by TIFPL found that the request received on February 2003 was fraudulent and the appellant's agent processed such request and a redemption cheque of 3.65 crores was handed over to a person on March 3, 2003. The appellant lodged a FIR on April 7, 2003 in MRA Marg Police Station. The appellant created a provision for embezzlement in the FY 2003-04 amounting to Rs.3.92 crores and accordingly vide a letter dated October 31st 2006 and claimed the provision as a loss in the AY 2004-05 which was denied. The*

*matter travelled to the Hon'ble ITAT and vide order ITA No.4990/Mum/2007 dated 11/8/2009, the Hon'ble Tribunal decided the allowability of embezzlement of loss. However, it observed that since the appellant had only created a provision in its, books of accounts, the contingent liability to fulfil in future cannot be allowed to the appellant in the year of creation of the provision and will thus, be allowed in the year of actual payment.*

*2.3.2 The appellant kept the demand alive for the claim of the provision on account of this embezzlement in the AY 2005-06 also. My Ld. Predecessor did not allow the claim on the same reasoning as indicated by the Hon'ble IT AT as referred supra. The appellant in the current year had paid to TIFPL an amount of Rs.4,42,73,539 vide cheque No.112500 dated 28/7/2006 as full and final settlement for the pending dispute. This payment was made against the opening provision of Rs.3.92 corers in. provided in the FY 2004-05. The appellant in fact paid an extra amount of Rs.50,57,940 by debiting to the P&L account. The appellant accordingly claimed Rs.3,92,15,599 on payment basis and also Rs.50,57,940 which was paid to TIFPL on account of the interest accrued on such liability. The Ld. AO has allowed the claim of Rs.3.92 crores, however, did not allow the claim of Rs.50,57,940 on the ground that the appellant has filed suit against the various parties and therefore, the claim has not reached its finality. In my opinion, the Ld. AO has not properly appreciated the facts of the case. The fact that the appellant is pursuing for recovery from the fraudulent party is a subject matter between the appellant in conjunction with the State i.e. the Govt. and the fraudulent party, it has nothing to do with the settlement of dispute with the parties whose payment was due since long. The fact that the appellant had paid a sum of Rs.4,42,73,539 has not been denied by the Ld. AO. The appellant has reached the settlement after waiting so long and paid the final amount to M/s. TIFPL and finally settled the issue with TIFPL. However, it's pursuing the matter with the fraudulent parties and in case, there is recovery, it has to be treated as income in case if the same is over the above of the settlement amount paid to TIFPL. Therefore, the addition made by the Ld. AO cannot be sustained both in law and on facts and is accordingly deleted."*

Aggrieved, now the Revenue is in second appeal before the Tribunal.

9. We have heard rival contentions and gone through facts and circumstances of the case. We find that TIFPL made an investment with the assessee on 30/07/2002 and redemption was due on 05/02/2003. It was found on receipt of request for redemption by TIFPL that the request received on February 2003 was fraudulent, but assessee's

transfer agent processed such request and a redemption cheque of 3.65 crores was handed over to a person on 03/03/2003. The assessee lodged a FIR on 07/04/2003 in MRA Marg Police Station and also created a provision for embezzlement in the FY 2003-04 amounting to Rs.3.92 crores and accordingly claimed the provision as a loss in the AY 2004-05 which was denied. The matter travelled to the ITAT and vide order ITA No.4990/Mum/2007 dated 11/8/2009, the Tribunal decided the claim of embezzlement of loss against assessee by observing that the assessee had only created a provision in its, books of accounts, the contingent liability to fulfil in future cannot be allowed in the year of creation of the provision and will thus, be allowed in the year of actual payment. We find that the assessee kept the demand alive for the claim of the provision on account of this embezzlement in the AY 2005-06 also. The assessee in the financial year relevant to this assessment year paid to TIFPL an amount of Rs.4,42,73,539 vide cheque No.112500 dated 28/7/2006 as full and final settlement for the pending dispute. This payment was made against the opening provision of Rs.3.92 corers provided in the FY 2004-05. The assessee accordingly claimed Rs.3,92,15,599 on payment basis and also Rs.50,57,940 which was paid to TIFPL on account of the interest accrued on such liability. The AO has allowed the claim of Rs.3.92 crores, however, did not allow the claim of Rs.50,57,940 on the ground that the assessee has filed suit against the various parties and therefore, the claim has not reached its finality. We find that the assessee has been pursuing his claim with the Banking Ombudsman as well as filing of an FIR with the Police but no result was coming out of the same. The fact that the assessee had paid a sum of

Rs.4,42,73,539 has not been denied by the AO. The assessee has reached the settlement after waiting so long and paid the final amount to TIFPL and finally settled the issue with TIFPL. In the present case before us the assessee had pursued the matter and side by side made payment to TIFPL on account of redemption of debentures, which has rightly been paid to the legitimate party and claimed the same as deduction. In the given facts and circumstances, we are of the view that the CIT(A) has rightly allowed the claim of the assessee and we confirm the same. This issue of Revenue's appeal is dismissed.

10. In the result, appeal of assessee is allowed and that of Revenue is dismissed.

Order pronounced in the open court on 18/05/2016

Sd/-  
(RAJESH KUMAR)  
ACCOUNTNAT MEMBER  
Mumbai, Dated 18/05/2016

Sd/-  
(MAHAVIR SINGH)  
JUDICIAL MEMBER

Vm, Sr. PS

**Copy of the Order forwarded to :**

1. The Appellant ,
2. The Respondent.
3. The CIT(A)-
4. CIT
5. DR, ITAT, Mumbai
6. Guard file.

//True Copy//

BY ORDER,

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