

**आयकर अपीलिय अधिकरण, मुंबई न्यायपीठ , मुंबई ।**

**IN THE INCOME TAX APPELLATE TRIBUNAL "J" BENCH, MUMBAI**

**BEFORE SHRI C.N. PRASAD, JUDICIAL MEMBER AND**

**SHRI ASHWANI TANEJA, ACCOUNTANT MEMBER**

**आयकर अपील सं /I.TA No. 4022/Mum/2007**

**(निर्धारण वर्ष / Assessment Year: 2003-04**

M/s. J.B. Boda & Co. Pvt. Ltd., Maker Bhavan, 1, Sir V.T. Marg, Mumbai-400 020	<b>बनाम/</b> Vs.	The ACIT, CC-17 & 28, Aayakar Bhavan, Mumbai
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**आयकर अपील सं /I.TA No. 4107/Mum/2007**

**(निर्धारण वर्ष / Assessment Year: 2003-04**

The ACIT, CC-17 & 28, Aayakar Bhavan, Mumbai	<b>बनाम/</b> Vs.	M/s. J.B. Boda & Co. Pvt. Ltd., Maker Bhavan, 1, Sir V.T. Marg, Mumbai-400 020
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**स्थायी लेखा सं./जीआइआर सं./PAN/GIR No. AAACJ 2289F**

<b>(अपीलार्थी /Appellant)</b>	..	<b>(प्रत्यर्थी / Respondent)</b>
अपीलार्थी ओर से/ Assessee by:		Shri P.J. Pardiwalla
प्रत्यर्थी की ओर से/Revenue by:		Shri Ashish Heliwal

**सुनवाई की तारीख / Date of Hearing :03.03.2016**

**घोषणा की तारीख /Date of Pronouncement :27.05.2016**

**आदेश / O R D E R**

**PER C.N. PRASAD, JM:**

These are appeals by the assessee and the Revenue against the orders of the Ld. CIT(A)-IV, Mumbai dated 16.03.2007 pertaining to assessment year 2003-04.

**ITA No. 4022/M/07 – Assessee's appeal**

2. The first issue in the appeal of the assessee is that the Ld. CIT(A) erred in upholding Assessing Officer's view that since assessee is only a broker/agent for insurance and reinsurance in domestic/international market the damages arising on account of claim made by the clients of the insurance/reinsurance companies were not its liability. It was further contended that assuming his view as right nevertheless the loss ought to have been allowed on the ground of commercial expediency.

3. Brief facts are that assessee company is acting as a broker in international insurance and reinsurance filed its return of income on 1.12.2003 declaring total income of Rs. 1,74,04,947/-. The assessment was completed on 30.12.2005 u/s. 143(3) of the Act determining the taxable income at Rs. 11,57,35,350/-. While completing the assessment, the Assessing officer disallowed loss of Rs. 8,93,29,938/- claimed by the assessee being the claim paid by the assessee to General Insurance Corporation of India (GIC) holding that this amount cannot be allowed as a business loss. The Assessing Officer was of the view that assessee is not liable to pay these amounts to GIC as there is no legal obligation or contractual liability. Hence he disallowed the claim paid by the assessee holding that it is not a liability to the assessee.

4. On appeal, the Ld. CIT(A) confirmed the disallowance agreeing with the view of the Assessing Officer that the damages arising on account of the claim made by the clients of the

insurance/reinsurance companies are not its liability of the assessee which is only a broker. The liabilities are to be paid by the insurance/reinsurance companies only. The Ld. CIT(A) held that the claims paid by the assessee to GIC are not allowable expenses. The contentions of the assessee that these payments were made to GIC on commercial expediency and therefore allowable expenses or loss was also turned down by the Assessing Officer as well as the Ld. CIT(A).

5.1 The Ld. Counsel for the assessee Shri P.J. Pardiwalla hearing on behalf of the assessee referring to the submissions made before the Assessing Officer submits that Reliance Industries took out a combined package policy to insure all aspects of its business. The primary insurance company issuing the policy is "The New India Assurance Company Limited, Mumbai". "General Insurance Corporation of India(GIC)" on behalf of "The New India Assurance company Limited" and the market placed the surplus risk in the international market on direct basis and through brokers.

5.2. The Ld. Counsel submits that "Marsh" and the assessee company handled the facultative reinsurance placement of the above policy for the year 1999- 2000 and the renewal for this policy was due from 26/12/-2000. "AON" a reinsurance broker was assigned the task. Pursuant to that authority, "AON" broked the reinsurance to Zurich Re who wrote a 12½% line and to ACE Global Markets in London who wrote a 12½% line on 22/12/2000. In the meantime, however, "AON" themselves had difficulties in placing the reinsurance and on 21<sup>st</sup> December, "GIC' instructed the assessee again to place a proportion of the reinsurance. However, at that time

“Marsh” withdrew from the placement. Nonetheless, in recognition of the work done by the assessee on behalf of "GIC", "GIG" were prepared to agree to "Split the lines' written by Zurich Re and ACE so that a proportion of each line previously written on "AON's' slip would be written on a slip or slip's broked by the assessee. Specifically, it was contemplated that the assessee would pick up 2 ½ % from Zurich Re and 5% from ACE and that the lines written by those re-insurers on "AON" slips would sign down to 10% and 7 ½ % respectively. In the course there was some delay in GIC providing the appropriate letter of authority and ultimately the letter has come on 2.2.2001 when GIC wrote to the assessee stating that signed order of 7.50% for placement with ACE(5.00%) and Zurich Global Energy (2.50%) was made. The Ld. Counsel submits that around that time AON signed down the lines of Zurich and ACE on their placement from 12½% in each case to 10% and 7 ½% respectively. The object of doing so was to accommodate the parallel placement by assessee.

5.3. The Ld. Counsel submits that thereafter Zurich Re duly signed Boda's slip for 2 ½% but ACE have refused to do so, contending that no agreement had been made by them to write a 5% line on a slip placed by Boda, the assessee. The complication which had arisen was that on 26/01/01, the Gujarat earthquake occurred. By early February it was clear that "The New India Assurance Company Limited" and hence, GIC and its reinsurances were facing substantial claims from Reliance Industries:

5.4. The Ld. Counsel submits that the stand adopted by Ace placed the assessee in an awkward position vis-a-vis its client GIC/The New

India Assurance Company Limited". "The New India Assurance Company Limited" had forwarded the relevant premium on 08/02/01 you will appreciate that the assessee had passed the premium to M/s. ACE and the brokerage income arising of this transaction was also booked in the accounts of the assessee.

5.5. The Ld. Counsel submits that M/s. ACE have accepted this premium however with a condition that they were re-insurers w.e.f. July, 2001. After having paid the premium, GIC/"The New India Assurance Company Limited" pursued the assessee to issue its cover note for the 7½% or order which assessee was responsible for placing. The amount of GIC/"The New India Assurance Company Limited" claim as it relates to the 5% which Ace should have written was sought to be recovered by "The New India Assurance Company Limited" from assessee on the basis that if Ace had not signed the slip, that was assessee's problem and "The New India Assurance Company Limited" could not be involved in the same.

5.6. The Ld. Counsel submits that later on advice from instructing solicitors, the assessee settled GIC/"The New India Assurance Company Ltd claim and started to follow up with ACE for recovery of this amount from them.

5.7. The Ld. Counsel submits that it is to be appreciated that the assessee is in the business of re-insurance from past 5 decades. There are a reinsurance broker who collect premium from the Insured and after deducting their commission remit to the respective reinsurer. They also collect the claims from the reinsurers on behalf of

reinsured and remit the same to them. In the course of their business they get business from the big insurance companies in India like GIC, "The New India Assurance Company Limited" etc. It is a continuous relationship with such companies in India and the assessee cannot deny its liability on account of the claims which arise due to the reinsurance placed by them in the international market. In the normal course the assessee would have received the claim from the reinsurer and in turn would have passed over to M/s. GIC/ "The New India Assurance Company Limited". In the present case the reinsurer denied its liability, however the assessee could not refuse the Indian insurance companies as they had already paid premium to them on 08/02/01 along with brokerage due to the assessee which it has accounted for, as its income. The assessee, therefore made the payment which is nothing but a business expenditure/loss which the assessee had to incur to continue its business in India. Such payment is on account of commercial expediency and accordingly debited to the profit and loss account and claimed as expenditure. Further the income in form of brokerage out of this transaction is already accounted for in the books of the assessee.

5.8. The Ld. Counsel further submitted that the assessee is a broker and the income earned by it is "brokerage income". As a practice of this industry it is required of them to collect premiums/claims and after retaining their brokerage the premium is passed over to the various reinsurers/cedants. Premiums/claims can never partake the character of income in the books of the assessee and therefore such sums can never be treated as income in the hands of the assessee. The loss suffered by the assessee of Rs. 8.93 Crores is a business loss

and on recovery if any will be written back in the books. However it is never an income as far as the assessee is concerned. The payment of those sums to "The New India Assurance Company Limited" is during the F. Y.2002-03 and is debited to the profit and loss account for the year in which it is incurred. This loss is incurred in carrying out the business of the assessee and is therefore a business loss. In order to continue to be in business in India it was essential to pay up the amounts to "The New India Assurance Company Limited" as otherwise it would have affected the business of the assessee adversely. Perhaps the loss on account of not receiving future business from such Indian Insurance Companies would affect the business' unfavourably and the assessee would face losses due to reduction in business. It was decided to pay up and retain its position in the Indian Market as the assessee felt that it would make good the same from M/s. ACE or then from the future business from the Indian market. By not paying, the future of the assessee in India would be bleak and its past reputation was at stake. The loss suffered by assessee to be in business is therefore a commercial loss which should be allowed to the assessee.

5.9. The Ld. Counsel further submits that the claim of the assessee was made to retain the business from GIC as the assessee is getting brokerage income from NIA/GIC around 45% of its brokerage annually and on average. Therefore, he submits that in view of commercial expediency, the claims were settled by the assessee to GIC and in turn claims were made on ACE Global Market. The Ld. Counsel for the assessee further submits that as a commercial

expediency if assessee bears a loss, it has to be allowed as deduction. For this proposition, he places reliance on the following decisions:

1. CIT Vs Naintal Bank Ltd. (62 ITR 638)
2. CIT Vs Sales Magnesite (Pvt.) Ltd (214 ITR 01)
3. SBI Funds Management Pvt. Ltd Vs ACIT in ITA No. 4001/M/02 dated 27.6.2007.

5.10. The Ld. Counsel for the assessee further referring to page 60 & 67 of the Paper book the computation of income for Assessment Year 2008-09 submits that during the assessment year 2008-09, the assessee has received Rs. 4,58,90,061/- from the foreign reinsurers in part settlement of claim of Rs. 8.33 crores. He submits that this amount was not considered as income in the computation for the Assessment Year 2008-09, since the assessee claimed loss of Rs. 8.33 crores in the Assessment Year 2003-04 which is under consideration, therefore, he submits that this amount should be reduced from the disallowance of Rs. 8,93,29,938/-. Therefore he submits that only balance may be directed to be allowed as business loss for the Assessment Year 2003-04.

6. The Ld. Departmental Representative vehemently supports the orders of the lower authorities. He submits that it is not the liabilities of the assessee to settle the claims and therefore loss cannot be allowed. In so far as the contention of the assessee that out of this amount of Rs. 8.33 crores, the assessee has received Rs. 4,58,90,061/- and only the balance should be considered for

allowance, the Ld. Departmental Representative submits that this may be restored for verification.

7. We have heard the rival contentions, perused the orders of the authorities below and the case laws relied on by the assessee. The Assessing Officer disallowed the claims paid by the assessee to GIC observing that there is no contractual obligation on the part of the assessee to make such payments. The Assessing Officer held that the claims of the assessee that it should be allowed as business loss has to be rejected. The contention of the assessee was that the claims were settled due to commercial expediency and therefore it should be allowed. The Ld. CIT(A) affirmed the disallowance rejecting the contention of the assessee that payments made by it are due to commercial expediency though there is no obligation on the part of the assessee. The only question before us is now to address as to whether the claims made by the assessee to GIC are due to commercial expediency and therefore allowable business expense/loss in the circumstances of the present case. The assessee is a broker for re-insurance has accepted the claim of GIC on the claims of its customers though the reinsuror ACE refused the liability and it is the contention of the assessee that the claims were settled by it keeping in view the business relations with GIC and to keep good relations with GIC which provides substantial business to the assessee. It is the contention of the assessee that assessee is receiving brokerage from GIC at an average percentage of 45 out of total brokerage. The details of brokerage earned from GIC/NIA for the last three assessment years is given as under:

A.Y.	Brokerage income from NIA/GIC	Brokerage income from others	Total brokerage	Percentage of brokerage income from NIA/GIC
2001-02	3,77,07,167	5,25,41,74	9,02,48,911	41.78%
2002-03	5,62,83,356	9,36,09,736	14,98,93,092	37.5%
2003-04	10,61,71,010	8,76,79,491	19,38,50,501	54.77%
			Average	45%

Therefore, it is the contention that the claims made by the assessee should be allowed as business loss to the assessee on commercial consideration as it was made to protect and preserve the business of the assessee with GIC in future.

8. In the case of CIT Vs Sales Magnesite (Pvt.) Ltd.,(214 ITR 01) the Jurisdictional High Court in the contest of deciding whether an expenditure has been incurred for the purpose of business and allowable as deduction u/s. 37 of the I.T. Act held as under: -

*“We have carefully considered the facts of the case. We have also noted the finding of the Tribunal that the payment made by the assessee to its sole selling agents as compensation for termination of the sole selling agency was a business expenditure which was incurred by the assessee after proper consideration of the facts and circumstances of the case and on the basis of legal opinion of its solicitors. The Tribunal has also recorded a clear finding of fact that the payment was made for commercial expediency. In view of this clear finding that the payment for termination of the sole selling agency was wholly on business considerations, we do not find any cogent reason to hold that the claim of the assessee was not allowable as business deduction.*

*The principles governing the allowance of deduction in respect of such expenditure were well settled by now by a catena of decision of the Supreme Court and the various High Courts. Such*

*deductions are ordinarily claimed and allowed under section 37 of the Act which is a residuary section extending the allowance of deduction to items of business expenditure not covered by any of the preceding section (section 30 to 36) and section 80VV. The only conditions are that: (i) it is not an expenditure, (a) in the nature of capital expenditure, or (b) personal expenses of the assessee, and(ii) it is laid out or expended wholly and exclusively for the purposes of the business or profession.*

*Various tests have been evolved by the courts from time to time to decide whether an expenditure is incurred for the purposes of business. One of the tests often applied is whether it is incurred by the assessee in his character as a trader. To hold it to be an expenditure allowable as a deduction under section 37, it is not essential that it should be necessary legally or otherwise, to incur the same or that it should directly and immediately benefit the business of the assessee. Even expenditure incurred voluntarily on the ground of commercial expediency and in order indirectly to facilitate the carrying on of the business would be deductible under this section. The question whether it was necessary for commercial expediency or not is a question that has to be decided from the point of view of the businessman and not by the subjective standard of reasonableness of the Revenue. As observed by the Supreme Court in *Bombay Steam Navigation Co. (1953) Pvt. Ltd. vs. CIT (1965) 56 ITR 52*, the question must be viewed in the larger context of business necessity or commercial expediency. No abstract or pedantic view can be taken in the matter.*

*Applying these tests to the facts of the present case, it is clear that the payment of compensation made by the assessee to its erstwhile sole selling agents for loss of the sole selling agency is allowable as a deduction under section 37 of the Act in the computation of income of the assessee”.*

9. In the case of *SBI Funds Management Pvt. Ltd Vs ACIT* in ITA No. 4001/M/02 dated 27.6.2007, the co-ordinate bench of this Tribunal after considering the decision of the Hon'ble Supreme Court in the case of *CIT Vs Naintal Bank Ltd. (62 ITR 638)* observed as under:

*We find that a somewhat materially identical situation came up before a Co-ordinate Bench of this Tribunal in the case of GIC Asset Management Co. Ltd., Vs ACIT (ITA No. 479/M/02 order dated 29<sup>th</sup> September, 2003) and one of us, i.e. the Accountant Member, was also present in the quorum of the said bench. While dealing with the said matter, the co-ordinate bench, inter alia, took note of the material facts as follows:*

*“GIC Mutual Fund, while launching some schemes, had offered to the prospective investors certain assured returns. Earning was not upto the expectation. There was a shortfall. To meet the shortfall between the earning and the assured return, the assessee also an asset management company debited Rs. 27,71,49,620 towards shortfall .....*

*The Assessing Officer rejected the claim of the assessee on the ground that the rights and obligations of the assessee in respect of management of the schemes of the GIC Mutual Fund is set out in the Investment Management Agreement. There is no stipulation in the agreement that the assessee could be held liable to make good the loss of assured return to the investors. The Ld. CIT(A) confirmed the order of the Assessing Officer.*

*Taking note of these facts as also the assessee’s basic contention that the shortfall was met “to preserve the business reputation and to preserve its primary source of business”, the Tribunal inter alia observed as follows:*

*..... Acting as investment manager of the GIC Mutual Fund was the primary and sole business of the assessee. Pending the decision to meet the shortfall, the reputation of the assessee was at stake .....*

*Looking around to the scheme of Mutual Fund, we find that the sponsorer gets nothing directly out of the income of the Mutual Fund. It only gets dividend if declared by the AMC. As such, sponsorer indirectly contributes towards the expenditure. Trustee gets onlys the sitting fees. The trust is created to make Mutual Fund a separate legal entity. Trustees are not responsible for*

*management of the Fund. It is the responsibility of the AMC. To discharge this responsibility, AMC gets professional charges. Therefore, AMC agreed to make good the loss to preserve the business reputation and primary sources of business.*

*It is well settled that the expenditure for preservation or protection of business asset is revenue expenditure. Even though there is no legal obligation to incur expenditure, if it is incurred in the interest of business, i.e. for maintaining and preserving business connections and goodwill of the business, it can be allowed as business expenditure.*

*Having regard to the facts, we are of the opinion that in the present case, the assessee incurred the expenditure to preserve its primary source. As such, in our opinion, the expenditure incurred was incidental to the business of the assessee. It is an allowable expenditure. We direct the Assessing Officer to delete the addition made on this count.*

*In the present case also, the only business that the assessee was involved in was asset management and the SBI Mutual Fund was its only client. In case the reputation or market standing of the Mutual Fund was to suffer, the only loser would have been the assessee. The Mutual Fund does not have any funds of its own, nor does it make any profits. The success of mutual fund gives rise to the profits in the hands of the asset management company. The only source of income in the hands of the assessee company is business of the SBI Mutual Fund. The expenditure incurred by the assessee is to preserve and protect its source of income. This becomes all the more clear from the memorandum to the board of directors, a copy of which is placed at paper book pages 119 to 122. The said memorandum takes note of the fact that there were deficits, that repurchase offer commencement date is 1<sup>st</sup> February, 1997, that since scheme had been promoted as a regular income annual scheme, non -payment of dividend will result in heavy repurchases liquidation – more so as there are alternate investment opportunities. It was also*

*noted that a dividend of less than 12% may not be commercially prudent since investors currently have a plethora of investment avenues providing more than 12% return which include bank fixed deposits (11 to 14%, PSU Bonds (15 to 16%), corporate bonds and debentures (16 to 17.5%), finance company deposits (18 to 20%). It was also noted that a lower dividend will result in large number of investors going in for forcing repurchase of the units. It was also noted that reputation of SBI Mutual fund will also be at stake since competitors like UTI and LIC are paying higher dividends on their regular income schemes. This memorandum also too note of the apprehension that in case the shortfall is not met, asset management company (i.e. the assessee) will find it difficult to obtain SEBI permission to launch future income schemes with guaranteed returns and that in the absence of guaranteed income returns, the success of scheme will be doubtful. It was in this background that a policy decision was taken to ensure that shortfall is met by the assessee company. This expense was thus on commercial considerations and with a view to protect and preserve future incomes of the assessee company. No doubt in a case like this, the nexus between the expenditure and the benefit is not as direct but it is clearly and unambiguously discernable. In a case in which the reputation of the SBI Mutual fund is allowed to suffer, the assessee's income till also suffer because in that case assessee company will have no or at least lesser, funds to manage. The Mutual fund, as is noted in the Tribunal order, extracts from which are reproduced above, is not the economic beneficiary of the mutual fund business. The economic beneficiary is the asset management company. Therefore, any expenditure incurred by the assessee to maintain, preserve or enhance the market standing of SBI Mutual Fund*

10. The principles laid down by the decisions squarely applicable to the facts of assessee's case. In this case also, the assessee settled the claims to GIC in view of its commercial expediency in the sense to retain the business to keep good relations with GIC which is providing substantial business to the assessee. Therefore, we hold

that the loss claimed by the assessee has to be allowed as business loss. However, we find that in the Assessment Year 2008-09 the assessee received Rs. 4,58,90,061/- being part of amount from re-insurers out of the claims made by it. On a perusal of the computation of income for Assessment Year 2008-09 filed by the assessee which is at page-66 and 67 of the paper book, we find that assessee has given a note stating that an amount of Rs. 4,58,90,061/- has been received in part settlement of the claim and this has not been considered as income for Assessment Year 2008-09 for the reason that this has already been disallowed in the year under consideration. Thus, we are of the view that since assessee has received the claims from the reinsurers to the extent of Rs. 4,58,90,061/- atleast to this extent cannot be allowed as business loss. Therefore, we direct the Assessing Officer to exclude Rs. 4,58,90,061/- from amount of disallowance and the balance only to be considered as business loss and accordingly such business loss to be allowed as deduction in this assessment year.

11. The next issue in the appeal of the assessee is that the Ld. CIT(A) erred in confirming the addition of Rs. 40,09,079/- as brokerage income received on the basis of an alleged discrepancy without appreciating the actual facts.

12. Brief facts are that in the course of assessment proceedings, the Assessing Officer called information from GIC regarding the amount of brokerage received/receivable by the assessee for the financial year ending 31.3.2003 relevant to assessment year 2003-04. The GIC informed that the total amount of brokerage booked on account

of the assessee M/s. J.B. Boda Pvt. Ltd was Rs. 5,27,74,677/-. The Assessing Officer asked the assessee to reconcile the amount of brokerage received/receivable from GIC since the assessee has accounted for its profit & loss account only an amount of Rs. 4,87,65,598/- towards brokerage. The assessee contended before the Assessing Officer that the insurance companies while accounting the brokerage as expense they go on the basis of the statement of accounts of the cedant received during the respective financial year whereas the assessee as brokers account for this brokerage as its income on the basis of reasonable assurance of receipt of premium. It was contended that in some cases it would take several years for the premium to be received by broker due to various exchange control regulations of the cedant countries. It was further contended that income of a broker directly arises out of the premium and therefore the point of accrual of income in the hands of assessee company could arise with the reasonable certainty of receiving the premium from the cedents. The Assessing Officer not convinced with the explanation offered by the assessee, added the difference of Rs. 40,09,079/- as income of the assessee on the ground that the GIC booked the expenses in its books of account and therefore as a matching principle the income also should have been booked by the assessee during this assessment year.

13. On appeal, the Ld. CIT(A) sustained the addition accepting the contention of the Assessing Officer that booking of expenses and income is always done by adhering to the matching concept, therefore the assessee should have booked the brokerage as income the GIC booked the brokerage as expenses in its books of accounts.

14. The Ld. Counsel for the assessee referring to page-41 of the Paper book submits that assessee is a broker and its brokerage income is directly linked to the premium receivable. The Ld. Counsel for the assessee submits that it is a general practice of the brokers to account for the brokerage on the basis of the reinsurance premium settled by the Cedants as a part of reinsurance account balances. He submits that assessee had accounted Rs. 4,87,65,598/- towards brokerage alongwith the co-brokers share of brokerage during the financial year 2002-03. The Ld. Counsel for the assessee submits that Assessing Officer failed to appreciate that the difference could have arisen due to various factors like exchange rate fluctuation, rectifications in the transactions recorded etc. It is the submission of the Ld. Counsel that assessee has declared the income following the method of accounting consistently adopted by it year after year and the Assessing Officer could not have ignored this aspect. The Ld. Counsel submits that the GIC might have booked excess. The Ld. Counsel for the assessee further submits that in none of the assessment years this kind of addition was made except for the Assessment Years 2002-03 and 2003-04.

15. The Ld. Departmental Representative submits that the assessee was asked to furnish the reconciliation and there was no proper reply from the assessee as to why the difference should not be assessed as income, therefore the Assessing Officer assessed the difference in brokerage received/receivable from GIC of India as income of the assessee. He vehemently supports the orders of the lower authorities.

16. Heard rival contentions, perused the orders of the authorities below. The Assessing Officer in the course of assessment proceedings called for the brokerage received/receivable by the assessee from GIC of India and the GIC informed the Assessing Officer the brokerage booked on account of assessee company as on 31.3.2005 was Rs. 5,27,74,677/-. This was informed to the assessee and asked to reconcile the amount. It is the observation of the Assessing Officer that he has conveyed this figure to the assessee and was asked to reconcile the amount of brokerage received/receivable as per figure declared in the profit & loss account. The assessee furnished the reply stating that difference between these two figures is for the reason that insurance companies while accounting the brokerage as expense they do it on the basis of the statement of accounts of the cedent received during the respective financial year whereas brokers account for this brokers as its income on the basis of reasonable assurance of receipt of premium. We find some force in the submission of the assessee that simply because the GIC of India booked the expenses in its books of account, it is not automatic that assessee should record such brokerage as its income. The Assessing Officer should have examined the point of accrual of income to the assessee rather than going by the figures obtained by the GIC of India. It is the submission of the Ld. Counsel that this kind of addition was not made in any of the Assessment Years except 2002-03 & 2003-04 by the Assessing Officer. The method of recognising brokerage income is being consistently followed by the assessee and there is no change. This is not in dispute. In view of this, we are of the considered view that the Assessing Officer is not justified in

considering the difference as income of the assessee only during this Assessment Year. Thus, we delete the addition made towards difference in brokerage received/receivable.

17. The last ground of appeal of the assessee is that the Ld. CIT(A) grossly erred in upholding the disallowance of Rs. 12 lakhs paid to J.B. Boda Brothers Pvt. Ltd. out of professional fees account on the pretext that the assessee had failed to submit the details of services rendered to it.

18. Brief facts are that the Assessing Officer while completing the assessment disallowed Rs. 12,00,000/- under the head professional fees. The assessee was asked to file details of these fees and assessee submitted that these amounts were paid to the professional services rendered by the sister concern J.B. Boda Brothers Pvt. Ltd. It was further submitted that these professional fees was paid to make use of services of Shri O.P. Rana who is employed with J.B. Boda Brothers Pvt. Ltd. However not convinced with the submissions of the assessee, the Assessing Officer disallowed the said expenses on the ground that assessee did not indicate the nature of services rendered by sister concern. The Assessing Officer also found that Shri O.P. Rana is an employee of J.B. Boda Brothers Pvt. Ltd and his services are not utilized by that company but was specifically hired to render to its employer J.B. Boda Brothers Pvt. Ltd is not mentioned anywhere. Therefore, he concluded that there is no justification for the payment made to J.B. Boda Brothers Pvt. Ltd towards professional fees for the services said to have been rendered by Shri O.P. Rana and disallowed the same in the absence of any proof of services rendered.

19. On appeal the Ld. CIT(A) sustained the order of the Assessing Officer in disallowing the said expenses. The Ld. Counsel for the assessee reiterated the submissions made before the lower authorities. He further submits that it is only a salary reimbursement and Shri O.P. Rana rendered professional services to the assessee company though he was in the role of J.B. Boda Brothers Pvt. Ltd., since the services were utilized for the purpose of the business of the assessee, the said expenses are allowable.

20. The Ld. Departmental Representative vehemently supports the orders of the lower authorities. He further submits that there is nothing on record to suggest that Shri O.P. Rana attended services to the assessee or to J.B. Boda Brothers Pvt. Ltd., and therefore he submits the Assessing Officer is justified in disallowing the said expenses.

21. Heard both sides, perused the orders of the lower authorities. Here the very question of rendering of services of Shri O.P. Rana to the assessee is in dispute. The records before us show that the assessee failed to furnish the details or prove that Shri O.P. Rana had rendered services to the assessee company. Nothing has been brought on record by the assessee in this regard. In the circumstances, we uphold the order of the lower authorities and dismiss the ground of the assessee.

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

**ITA No. 4107/M/07 – Revenue’s appeal**

23. The only issue in the appeal of the Revenue is that the Ld. CIT(A) erred in deleting the disallowance of interest u/s. 36(1)(iii) of the Act.

24. The Assessing Officer in the course of assessment proceedings disallowed interest of Rs. 32,51,885/-. This amount consists of notional interest of Rs. 19,89,158/- on investments and notional interest of Rs. 11,66,982/- on advances made to sister concerns. These amounts were disallowed out of interest incurred by the assessee for the reason that assessee has not proved that investments were made out of its own funds and secondly assessee advanced interest free amounts to group concern.

25. On appeal the Ld. CIT(A) deleted the disallowance holding that assessee made advances for the purpose of business, investments were made on business compulsion and therefore, notional interest cannot be disallowed. He also held that notional interest on advance to sister concern also not disallowable in view of the decision of the Hon’ble Supreme Court in the case of S.A. Builders Ltd. Vs CIT (288 ITR 01).

26. The Ld. Departmental Representative places reliance on the order of the Assessing Officer in disallowing interest u/s. 36(1)(iii).

27. The Ld. Counsel for the assessee reiterated the submissions made before the lower authorities. The Assessing Officer disallowed

interest u/s. 36(1)(iii) on the ground that assessee made certain investments, tax free bonds and advances, interest free amounts to sister concern. This aspect of the matter has been elaborately considered by the Ld. CIT(A) with reference to the averments of the Assessing Officer and the submissions of the assessee and concluded that the investments were for the purpose of business due to commercial expediency and therefore the notional interest disallowed by the Assessing Officer is deleted by observing as under:

*9. In response to the AO's query dated 20.12.2005, the appellant stated that the investments had been made out of its own fund, but gave no proof thereof. The AO held that the investment are not for the business purpose and the disallowance of interest out of interest debited to Profit and Loss account is called for as per provisions of section 36(1)(iii) of the I.T.Act. Consequently, interest at the rate of 12% i.e. the average borrowing rate of the appellant during the year was disallowed on these investments. Further, as the investment in M/s J B Boda Insurance Pvt Ltd amounting to Rs.24,50,000/- and Rs.98,00,000/- has been made on 24.02.2003 and 24.01.2003 respectively, the disallowance of interest in respect of these investments was worked out on prorata basis. The working of the disallowance is given as under by the AO in the assessment order :-*

*"5.1.9. Since the investment in M/s. J.B.Boda Insurance Pvt. Ltd amounting to Rs. 24,50,000/- and Rs. 98,00,000/- have been made on 24.2.2003 and 24.01.03 respectively, the disallowance of interest in respect of these investments shall be worked out only for the period of investments during this financial year. The computation of interest which becomes disallowable in respect of these investments is worked out as under:*

Name	Amount of investment	Interest Disallowable
a)M/s. J.B. Boda & Co. Pvt. Ltd.	Rs. 86,16,320/-	10,33,958
b)M/s. J.B. Boda Insurance Brokers Pvt. Ltd (from 24.2.03 to 31.3.03)	Rs. 24,50,000/-	29,400
c) M/s. J.B. Boda Re-insurance Pvt. Ltd. (from 24/01/03 to 31/03/03)	Rs. 98,00,000/-	2,05,800
d) Konkan Railway Corpn. (10.5% tax free bonds)	Rs. 50,00,000/-	6,00,000
e) GIC Mutual Fund (GIC fortune 94)	Rs. 10,00,000/-	1,20,000
Total	Rs.2 ,68,66,320/-	19,89,158/-

*The appellant had, inter-alia, advanced loans to its group/ sister concerns. The examination of ledger accounts of the group/ sister concern show that while there was fluctuating debit and credit balances, in the case of J B Boda Brothers Pvt Ltd, it was only the debit balance which was being allowed to continue year after year.*

*A closer look at the ledger account of M/s. J.B.Boda and Bros. Pvt. Ltd. showed that it had opening debit balance of Rs. 85,36,897/- during the year it only increased and as on 31.3.03 there was a debit balance of Rs. 1,20,16,997/-. The total of all credit transactions in this ledger account through out the year comes to only Rs.24,48,701/- as against the additional debit entries during the year amounting to Rs. 59,28,801/- and hence the increase in the amount of debit balance.*

*Here it is important to note that the known business debit balance in favour of sister concern was allowed to not only continue but rather increase the amount of debit balance. In view of this, the assessee company was asked to work out the amount*

*of interest disallowable out of the interest debited to profit and loss account. (vide order sheet entry dated 20/12/105).*

*The appellant, vide letter dated 29.12.2005 worked out the disallowance of interest @ 10% p.a. aggregating Rs.972485/-. However, the AO stipulated that the rate of borrowing during the year was 12% and applying the rate of 12%, the disallowance was worked out to Rs.11,66,982/- instead of Rs.972485/-.*

*Further the Assessing Officer observed that the appellant company had paid interest of 12% on unsecured loans borrowed from the directors and their relatives whereas it was earning only 4.5% to 10% on various investments. The Assessing Officer intended to disallow the differential rate i.e. 2%. The appellant claimed that no interest is paid to any directors. The Counsel of the appellant brought to my notice that the appellant company had paid interest @ 12% to its shareholders whose funds were utilized by the appellant as and when needed and the directors shareholders of the company have their current account with the appellant and for which the interest @ 12% is paid to them. Also, the appellant company has no external borrowings and uses its own reserves and the balance of shareholder capital maintained by it for running business. Further, the shareholders, to whom interest is paid, have duly paid taxes on the receipt.*

8. *The AO rejected this explanation holding that the payment of interest, over and above the prevailing market rate and also at a rate that is much higher than the amount of return the appellant is getting on loans and advances, which it has given, including the investment made is not tenable. He thereafter, proceeded to disallow the differential rate of interest by adopting the rate of 2% out of the interest debited to the P&L account as in his opinion it amounted to giving undue benefit to its directors leading thereby to lowering taxable income.*

*The AO thereafter concluded, that the capital borrowed should have been invested in appellant's own business and the diversion of such borrowed capital should only be for business*

*purposes. He thereafter proceeded to disallow interest u/s.36(1) (iii) aggregating to Rs.3251885/-.*

9. *The submissions of the Ld. Counsel disputing the above observations and contention of the Assessing Officer are summarized as under :-*

*a) With regards to the notional interest @ 12% on investments made for business purposes, was purely for business purpose. The appellant to continue its business in India had to set-up two new companies for Insurance broking and reinsurance as per the "IRDA" regulation. Thus, the investment made in M/s J B Boda & Co., Singapore Pvt. Ltd., M/s J B Boda Insurance Co. Pvt Ltd and M/s J B Boda Reinsurance Co.Pvt Ltd was purely for business compulsion as per the regulations of IRDA.*

*b) The appellant company invested Rs.50.00 lacs in Konkan Railway Corporation Ltd which gave a return of 10.5% tax free interest and Rs.10.00 lacs in GIC Mutual fund. The Assessing Officer had wrongly disallowed notional interest of RS.6.00 lacs on the railway bonds without appreciating that the appellant company had received tax free income of Rs.525000/- on these investments. In addition, the Profit or loss arising on the sale of GIC Mutual fund would also be accounted for in the appellant 's books in the year of sale of such investments.*

*The appellant company is a parent company of J.B. Boda Group of company and consistently follows the method of incurring all management expenses and recovering them on the group concerns. The debit balance in the account of M/s. J.B. Boda Brothers Pvt. Ltd was due to management expenses recoverable from them and certain advances made for business purposes. Out of the four sister concerns of the appellant company there was a debit balance through out the year in the case of J.B. Boda Brothers Pvt. Ltd and a credit balance through out the year in the case of M/s. J.B. Boda Offshore Surveyors and Adjustors Pvt Ltd. In the case of Crow Boda & Co. Pvt. Ltd. the balance was partly debit and partly credit for the year. In the*

*case of J.B. Boda Surveyors Pvt Ltd, the account shows huge credit for a major part of the year . Since the appellant company has no external borrowings for running its business, the appellant had lent some sums to one of its group company at the same time it had borrowed from another group company also.*

*The Counsel for the appellant reiterated before me that no payment of any interest was made to the Directors. The interest paid by the appellant company is on the shareholders funds which are used for business purposes. The appellant company used these funds as and when required for the business needs. The appellant company had no external borrowings and uses its own reserves and the balance of share holders capital maintained with it for running its business. IN any case, if the appellant company had borrowed the funds from outside the borrowing rate is much higher as compared to the 12% which the appellant paid to its shareholders on their outstanding balance.*

*10. The arguments of the Ld. Counsel, disputing the addition of Rs. 32,51,885/- have been considered by me.*

*11. It is pertinent to point out at the outset, that in order to decide whether interest on funds borrowed by the appellant and given at lower interest or interest free to sister concerns or subsidiaries should be allowed as a deduction u/s. 36(1)(iii) of the I.T. Act, 1961, one has to keep the larger question in mind i.e. whether the loan was given by the appellant as a measure of commercial expediency. The Hon'ble Supreme Court of India in the case of S.A. Builders Ltd Vs CIT & Another as reported in 288 ITR page 1 has elaborated the expression "Commercial Expediency". To quote the Hon'ble Supreme Court*

*"The expression "commercial expediency" is one of wide import and includes such expenditure as a prudent businessman incurs for the purpose of business. The expediency may not have been incurred under any legal*

*obligation, but yet it is allowable as business expenditure if it was incurred on grounds of commercial expediency.*

*Decisions relating to section 37 will also be applicable to section 36(1)(iii) because in section 37 the expression used is 'for the purpose of the business'. For the purpose of business" includes expenditure voluntarily incurred for commercial expediency, and it is immaterial if a third party also benefits thereby.*

*To consider whether one should allow deduction u/s 36(1) (iii) of interest paid by the assessee on amounts borrowed by it for advancing to a sister concern, the authorities and the courts should examine the purpose for which courts should examine the purpose for which the assessee advanced the money and what the sister concern did with the money. That the borrowed amount is not utilized by the assessee in its own business but had been advanced as interest free loan to its sister concern is not relevant. What is relevant is whether the amount was advanced as a measure of commercial expediency and not from the point of view whether the amount was advanced for earning profit.*

*Once it is established that there was nexus between the expenditure and purpose of the business (which need not necessarily be the business of the assessee itself) the Revenue cannot justifiably claim to put itself in the arm - chair of the businessman or in the position of the board of directors and assume the role to decide how much is reasonable expenditure having regard to the circumstances of the case. No businessman can be compelled to maximize his profits.*

*We agree with the view taken by the Delhi High. Court in CIT Vs. Dalmia Cement (B) Ltd (2002) 254 ITR 377 that once it is established that there was nexus between the expenditure and the purpose of the business (which need*

*not necessarily be the business of the assessee itself), the Revenue cannot justifiably claim to put itself in the arm-chair of the businessman or in the position of the board of directors and assume the role to decide how much is reasonable expenditure having regard to the circumstances of the case. No businessman can be compelled to maximize his profit. The income-tax authorities must put themselves in the shoes of the assessee and see how a prudent businessman would act. The authorities must not look at the matter from their own view point but that of a prudent businessman. As already stated above, we have to see the transfer of the borrowed funds to a sister concern from the point of view of commercial expediency and not from the point of view whether the amount was advanced for earning profits.*

*We wish to make it clear that it is not our opinion that in every case interest on borrowed loan has to be allowed if the assessee advances it to a sister concern. It all depends on the facts and circumstances of the respective case. For instance, if the directors of the sister concern utilize the amount advanced to it by the assessee for their personal benefit, obviously it cannot be said that such money was advanced as a measure of commercial expediency. However, money can be said to be advanced to a sister concern for commercial expediency in many other circumstances (which need not be enumerated here). However, where it is obvious that a holding company has a deep interest in its subsidiary and hence if the holding company advances borrowed money to a subsidiary and the same is used by the subsidiary for some business purposes, the assessee would, in our opinion, ordinarily be entitled to deduction of interest on its borrowed loans.*

*It is clear from the judgement of Hon'ble Supreme Court (supra) that the expression "for the purpose of business" is wider in scope than the expression "for the purpose of earning profit". The facts of the case pertaining to the appellant which have been*

*elaborately discussed in the assessment order and also in the submissions made during the assessment proceedings would lead to the infallible contention that the disallowance made by the Assessing Officer is founded on conjectures and surmises. Section 36(1)(iii) does not give power to draw presumption in regard to working out the disallowance of notional interest. The balance of probabilities weighs in favour of the appellant and I therefore, delete the addition of Rs. 32,51,885/- on account of notional interest u/s. 36(1)(iii) of the I.T. Act.”*

The above findings of the Ld. CIT(A) have not been controverted by the Revenue. In the circumstances, we agree with the view of the Ld. CIT(A) that the investments made by the assessee are for the purpose of business due to commercial expediency and no interest on notional basis could be disallowed. Thus, we sustain the order of the Ld. CIT(A) and dismiss the Revenue's appeal.

28. In the result, the appeal filed by the assessee is partly allowed and the appeal filed by the Revenue is dismissed

Order pronounced in the open court on 27<sup>th</sup> May, 2016.

Sd/-

Sd/-

**(ASHWANI TANEJA)**

**(C.N. PRASAD )**

लेखा सदस्य / ACCOUNTANT MEMBER

न्यायिक सदस्य/JUDICIAL MEMBER

मुंबई Mumbai; दिनांक Dated : 27<sup>th</sup> May, 2016

व.नि.स./ Rj , Sr. PS

**आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :**

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent.
3. आयकर आयुक्त(अपील) / The CIT(A)-
4. आयकर आयुक्त / CIT
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण,  
मुंबई / DR, ITAT, Mumbai
6. गार्ड फाईल / Guard file.

**आदेशानुसार/ BY ORDER,**

सत्यापित प्रति //True Copy//

**उप/सहायक पंजीकार**

(Dy./Asstt. Registrar)

**आयकर अपीलीय अधिकरण, मुंबई / ITAT, Mumbai**