

आयकर अपीलीय अधिकरण, मुंबई न्यायपीठ 'जी' मुंबई ।

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

**सर्वश्री जी.ई.वीरभद्रप्पा, अध्यक्ष, एवं श्री अमित शुक्ला, न्या.स. के समक्ष ।
BEFORE SHRI G.E. VEERABHADRAPPA, HON'BLE PRESIDENT
AND SHRI AMIT SHUKLA, JUDICIAL MEMBER**

आयकर अपील सं./ ITA No.7478/Mum/2010.

(निर्धारण वर्ष / Assessment Year: 2007-2008)

Global Innovsource Search Solutions P. Ltd., A-203, Kailash Indl. Complex, Park Site, Vikhroli (W), Mumbai-400 079.	Vs.	ITO 10(2)(3), Mumbai
स्थायी लेखा सं./जीआइआर सं./PAN No. AABCI 2738 P		
(अपीलार्थी /Appellant)	:	(प्रत्यर्थी / Respondent)

एवं/ AND

आयकर अपील सं./ ITA No.9245/Mum/2010

(निर्धारण वर्ष / Assessment Year: 2007-2008)

ITO 10(2)(3), Mumbai	Vs.	Global Innovsource Search Solutions P. Ltd., A-203, Kailash Indl. Complex, Park Site, Vikhroli (W), Mumbai-400 079.
स्थायी लेखा सं./जीआइआर सं./PAN No. AABCI 2738 P		
(अपीलार्थी /Appellant)	:	(प्रत्यर्थी / Respondent)

निर्धारिती की ओर से / Assessee by

Mr. K.Shivaram

:

राजस्व की ओर से/ Revenue by

Mr. Parthsarathi

:

सुनवाई की तारीख / Date of Hearing : 21st June 2012

घोषणा की तारीख /Date of Pronouncement :27th June, 2012

आदेश / ORDER

PER AMIT SHUKLA (J.M.) :

These are the cross appeals filed by the assessee as well as the department against the order dated 18-8-2010, passed by the CIT (A)-

21, Mumbai for the quantum of assessment passed under Section 143(3) for the assessment year 2007-2008. In both the appeals, the issues are common which relates to disallowance of Rs.20,00,000/- made by the Assessing Officer towards reimbursement of expenses after invoking the provisions of Section 40A(2(b)). The CIT(A) has given part relief for Rs.10,00,000/- against which both the parties are in appeal.

2. The relevant facts in brief are that the assessee company is a wholly owned subsidiary of Innovsource Solutions Pvt. Ltd. and is engaged in the business of providing staffing service. The Company's parent i.e. holding company is engaged in providing recruitment services. The Assessing Officer on going through the audited accounts, noticed that the assessee has claimed reimbursement of expenditure of Rs.51,01,810/- which was shared by the parent company. Before the Assessing Officer detail submissions along with documentary evidence were placed, in support of the expenses which was shared with the parent company. It was explained before him that certain resources like staff, office premises etc. have been used commonly both by the assessee company and its parent company, the expenses relating to these resources have been shared by the assessee company. This reimbursement of the share of expenses is evidenced by a written 'memorandum of understanding' between them. It was also brought to the notice of the Assessing Officer that

the assessee's case in the preceding year i.e. AY 2006-2007 was completed under Section 143(3), wherein such a reallocation and reimbursement of expenses have been accepted. The Assessing Officer rejected the claim of the assessee and held that expenses incurred by the parent company cannot be held to be wholly and exclusively for the purpose of the business and held that as per Section 40A(2)(b), the assessee is required to prove that expenses incurred through associate companies are reasonable and at arms length, considering the services rendered by the assessee. Since the assessee has failed to discharge the onus to prove the reasonableness of the expenditure, a sum of Rs.20,00,000/- was disallowed out of ₹.51,01,810/- considering it to be unreasonable and excessive.

3. Before the CIT(A), the assessee objected to the observations and findings of the Assessing Officer on various counts. The submissions made before the CIT(A) have been incorporated at page 2 & 3 of the appellate order. The sum and substance of the said arguments are that :-

- i) The assessee is conducting the business activities from the premises which have been taken on rent by the parent company and the expenses shared are mainly overhead expenses. The expenses pertaining to both the parent and the assessee company have been identified as per the

agreed norms given in the memorandum of understanding and such identified expenses were only to be shared and then it was subject to reimbursement.

- ii) The only expenses benefiting both the companies were identified and was shared as per the mutually agreed terms and such a sharing of expenses arose since the resources were belonging to the parent company which was incorporated earlier to the assessee company.
- iii) As per Section 40A(2)(b) only expenditure incurred in respect of which payment has been made to specified persons, which in the opinion of the Assessing Officer, is reasonable, can be disallowed, which in the case of the assessee will not apply as the expenditure has been incurred by the parent company and the assessee has simply reimbursed such expenses. There is no question of applying 40A(2)(b). The reimbursement was done on actual basis. It is not a case where parent company was rendering any service for which payment has been made by the assessee.
- iv) The entire arrangement of sharing of expenses is devoid of any tax consideration and is solely based on and guided by contractual arrangement and commercial and factual consideration. Therefore, such an adhoc disallowance is not called for.

4. The CIT(A) accepted the contentions of the assessee and admitted that parent company had incurred cost for sharing of common office premises, staff etc. by the assessee and such expenses are attributable to the assessee company which amounts to Rs.51,01,810/-. The CIT(A) has noted down the following details of expenses :-

Consulting Charges	Rs. 4,79,801/-
Business Promotion expenses	Rs. 36,779/-
Advertisement and media publicity	Rs. 71,567/-
Job drive, site expenses	Rs. 14,368/-
Membership and subscription	Rs. 13,233/-
Leaseline Expenses	Rs. 3,06,347/-

Salaries and Wages	Rs. 33,98,293/-
Rent, rates and taxes	Rs. 1,91,910/-
Printing and stationery	Rs. 85,049/-
Travelling and conveyance	Rs. 77,636/-
Electricity charges	Rs. 1,09,030/-
Office upkeep and maintenance	Rs. 95,244/-
Telephone expenses	Rs. 99,460/-
Miscellaneous expenses	Rs. 21,057/-

and found that expenses above the line have not been debited in the profit loss account. This goes to prove the assessee's case that it was sharing expenses with the parent company on these expenses. The expenses below the line was found to be incurred for the branches located in the other cities. Even after accepting the assessee's contention, that the expenditure incurred by the parent company were also benefiting the assessee's business and the assessee was required to share/reimburse those expenses, however, held that the entire expenses cannot be held to be allowable. The reasoning given

by the CIT(A) is that if the salary and allowance expenses of Rs.11.86 crores have been incurred by the assessee itself, then what was the need of using the parent company employees for which amount of Rs.33.98 lacs was reimbursed. He was of the opinion that there was no criteria to measure the extent of benefit obtained by the assessee on account of expenses incurred by the parent company. Both the assessee's claim and the Assessing Officer, disallowance are based on ad hoc basis, therefore, some disallowance is called for in this case. On this reasoning, he confirmed the disallowance at Rs.10,00,000/- under Section 40A(2)(b).

5. Before us, learned counsel for the assessee submitted that when the entire reimbursement of expenses are based on 'memorandum of understanding' and without pointing out any unreasonableness or excessiveness in any of the heads of reimbursement of expenses, no disallowance could have been made. He reiterated most of the submissions which were made before the CIT(A). On the other hand, learned Senior DR submitted and element of excessiveness or unreasonableness cannot be ruled out in the business as there are no instance of comparable case with the unrelated parties. He though strongly relied upon the reasoning and the observation of the CIT(A), however, submitted that the relief given by the CIT(A) at Rs.10,00,000/- is uncalled for on the facts and circumstances of the case.

6. We have carefully considered the rival submissions and also perused the material placed on record and the findings of the CIT(A). Under the provisions of section 40A(2)(a), it is clear that payments which have made to a person specified in sub clause (b) of sub section 2 of section 40A, the reasonableness of the expenditure has to be judged as per the conditions provided therein. Section 40A (2)(a) reads as under :-

“(2)(a) Where the assessee incurs any expenditure in respect of which payment has been or is to be made to any person referred to in clause (b) of this sub-section, and the [Assessing] Officer is of opinion that such expenditure is excessive or unreasonable having regard to the fair market value of the goods, services or facilities for which the payment is made or the legitimate needs of the business or profession of the assessee or the benefit derived by or accruing to him therefrom, so much of the expenditure as is so considered by him to be excessive or unreasonable shall not be allowed as a deduction.”

From the plain reading of above, it is amply clear that the payments which are made to persons specified in sub-clause b of sub section 2 of Section 40A, if in the opinion of Assessing Officer, is excessive and unreasonable;

firstly, having regard to the fair market value of the goods, services or facilities for which the payment is made;

secondly, looking to the legitimate needs of the business or profession of the assessee;

or **thirdly**, the benefit derived by or accruing to him therefrom;

These three are alternative tests and the same do not necessary prohibit consideration of other circumstances. Even though section provides for subjective satisfaction of the Assessing Officer qua allowability of the payment, but it has to be examined keeping in mind the goods, services or facilities provided by the related persons for which payment is made. In such a process, the legitimate needs of the business or profession of the assessee or benefit derived by or accruing to the assessee has to be kept in mind. After applying this test, if it is found that the expenditure is excessive or unreasonable, then excess or unreasonable portion of the expenditure is to be disallowed. For invoking provision of Section 40A(2)(b), the Assessing Officer has to bring some cogent material or facts on record that the payment is excessive or unreasonable either having regard to the fair market value of goods and services or legitimate needs of the business. The Assessing Officer has to prove that the transaction is sham or not bonafide or the value of goods and services are not in consonance with the fair market value.

6.1 Here in this case, it is not disputed fact that the assessee is sharing staff, office premises, etc. with its parent company. The allocation of the expenses have been identified as per the memorandum of understanding with regard to nature and the quantum of expenses which were to be borne out by the parent company and to be reimbursed by the assessee. Nowhere the

Assessing Officer has spelled out as what were the expenses, which have been reimbursed are unreasonable or excessive looking to the fair market value of the services and expenses reimbursed. Even the reasoning of the CIT(A) on reimbursement of salary expenses that they are excessive in view of the fact that the assessee company has itself incurred salary and allowances expenses at Rs.11.86 crores, cannot be the ground for any disallowance as nowhere it has been brought on the record as to how the reimbursement of 33.98 crores on salary account for use of parent company's employees is unreasonable or excessive. To draw any adverse inference under Section 40A(2)(a), there has to be some concrete evidence or material to allocate the unreasonable and excessive expenses for the purpose of disallowance under Section 40A(2)(a). Once, the CIT(A) has come to the conclusion that arrangement of expenses is correct and bonafide and is in accordance with the terms of agreement between both the parties, then no ad hoc disallowance of any amount is called for. Thus, we do not find any reason to sustain any portion of the disallowance under Section 40A(2)(a). Accordingly the grounds raised by the assessee is allowed and that of department is dismissed.

7. In the result, the appeal of the assessee is allowed and the appeal of the revenue is dismissed.

परिणामतः निर्धारिती की अपील स्वीकृत की जाती है एवं राजस्व की अपील खारिज की जाती है ।

Order pronounced in the open court on 27th June, 2012 .

आदेश की धोषणा खुले न्यायालय में दिनांक: 27th June,2012 को की गई ।

Sd/-
(जी.ई.वीरभद्रप्पा)
(G.E. VEERABHADRAPPA)
अध्यक्ष / PRESIDENT

Sd/-
(अमित शुक्ला)
(AMIT SHUKLA)
न्यायिक सदस्य/JUDICIAL MEMBER

मुंबई Mumbai; दिनांक Dated 27th / June /2012

प्र.कु.मि/pkm.नि.स./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.

सत्यापित प्रति //True Copy//

आदेशानुसार/ BY ORDER,

उप/सहायक पंजीकार
(Dy./Asstt. Registrar)
आयकर अपीलीय अधिकरण, मुंबई / ITAT, Mumbai