

IN THE INCOME TAX APPELLATE TRIBUNAL
"B" Bench, Mumbai
Before Shri B.R. Baskaran (AM)& Shri Pawan Singh (JM)

I.T.A. No. 5289/Mum/2015 (Assessment Year 2010-11)
I.T.A. No. 5290/Mum/2015 (Assessment Year 2011-12)

Dy. CIT, Circle-2(2)(2) Room No. 549 Aayakar Bhavan M.K. Road Mumbai-400 020.	Vs.	M/s. Morgan Stanley (India) Capital Pvt. Ltd. 18F/19F, B-Wing Tower-2, One Indiabulls Centre, Jupiter Mill Compound, 841 S.B. Marg, Elphinstone Road, Mumbai-400013.
(Appellant)		(Respondent)

I.T.A. No. 4962/Mum/2015 (Assessment Year 2010-11)
I.T.A. No. 4963/Mum/2015 (Assessment Year 2011-12)

M/s. Morgan Stanley (India) Capital Pvt. Ltd. 18F/19F, B-Wing Tower-2, One Indiabulls Centre, Jupiter Mill Compound, 841 S.B. Marg, Elphinstone Road, Mumbai-400013.	Vs.	Dy. CIT, Circle-2(2) Room No. 549 Aayakar Bhavan M.K. Road Mumbai-400 020.
(Appellant)		(Respondent)

PAN : AABCB4845Q

Assessee by	Shri Sunil Moti Lala & Shri Tushar Hathi Ramani
Department by	Shri T.A. Khah
Date of Hearing	29.01.2018
Date of Pronouncement	29.01.2018

ORDER

Per Bench :-

These cross appeals are directed against the orders passed by the learned CIT(A)-5, Mumbai and they relate to A.Ys. 2010-11 & 2011-12. All

these appeals were heard together and hence they are being disposed of by this common order, for the sake of convenience.

2. The assessee herein is registered as a non-deposit taking non-banking financial company with Reserve Bank of India and is classified as “Loan and Investment Company”. During the years under consideration, the assessee was primarily engaged in making investments in corporate/government bonds, certificate of deposits, commercial papers, pass through certificates, IPO funds, loans secured against assets and other securities based lending.

3. We shall first take up the appeal filed by the Revenue for A.Y. 2010-11. First issue contested therein relates to disallowance made u/s. 14A of the Act. During the year under consideration, the assessee received dividend income of ₹ 4,87,200/-. The assessee suo-moto disallowed a sum of ₹ 5,90,507/- u/s. 14A of the Act. The Assessing Officer, however, computed the disallowance by applying provisions of Rule 8D of the I.T. Rules which worked out to ₹ 125.43 lakhs. Accordingly he enhanced the disallowance u/s 14A to Rs.125.43 lakhs.

4. Before the learned CIT(A), the assessee submitted that the own funds available with it is more than the value of investment and hence no disallowance u/r. 8D(2)(ii) out of interest expenditure is called for. The assessee also submitted that the disallowance made by it would meet requirements of Rule 8D(2)(iii). The learned CIT(A) was convinced with the contentions of the assessee and accordingly deleted enhancement made by the Assessing Officer.

5. The Learned Departmental Representative placed strong reliance on the order passed by the Assessing Officer.

6. On the contrary, the learned AR submitted that the disallowance u/s. 14A should not exceed dividend income as held by Hon'ble Delhi High Court in the case of Joint Investments Pvt. Ltd. (2015) 59 Taxman 295. He submitted that an identical issue was considered by the Coordinate Bench of the Tribunal

in one of the sister concerns of the assessee named M/s. Morgan Stanley India Co. Pvt. Ltd. (ITA No. 1576/Mum/2016 dated 20.12.2017), wherein the Coordinate Bench followed the decision rendered by another Coordinate Bench in the case of Pest Control India Pvt. Ltd. Vs. DCIT (ITA No. 5048/Mum/2016 dated 31.10.2017) and held that the disallowance u/s. 14A should not exceed the amount of exempt income. In this regard, the Coordinate Bench has followed the decision rendered by Hon'ble P&H High Court in the case of Principal Commissioner of I.T. Vs. Empire Package Pvt. Ltd. (ITA No. 415 of 2015 dated 12.1.2016). Accordingly he submitted that the order passed by Ld CIT(A) on this issue does not call for any interference.

7. Having heard the rival submissions, we are of the view that the order passed by the learned CIT(A) does not call for any interference. The learned CIT(A) has observed that share capital and reserves available with the assessee was ₹ 768 crores while the value of investments made by the assessee was ₹ 81 crores. Hence, the learned CIT(A) has followed the decision rendered by Hon'ble Bombay High Court in the case of CIT Vs. HDFC Bank Ltd. (366 ITR 505), wherein it was held that no disallowance out of interest expenditure is called for when own funds available with the assessee exceeds value of investment. The learned CIT(A) has further observed that the disallowance as per Rule 8D(2)(ii) works out to ₹ 1,86,773/-, while the assessee itself has disallowed a sum of ₹ 5,90,507/-. It is also pertinent to note that the actual amount of exempt income earned by the assessee was lower than the amount disallowed by the assessee u/s 14A of the Act. Hence, the decision rendered by the Coordinate Bench in the case of Morgan Stanly Co. Pvt. Ltd. (supra) squarely applies to the facts of the present case. In view of the forgoing discussions, we are of the view that the order passed by the learned CIT(A) on this issue does not call for any interference.

8. The next issue contested by the Revenue relates to disallowance made u/s. 40(a)(ia) of the Act. The Assessing Officer noticed that the assessee has reimbursed amounts towards “advertisement and general expenses” to various

group companies on the basis of cost sharing arrangement entered with them. The amount so reimbursed was ₹ 2230.48 lakhs. The assessee had deducted tax at source u/s. 194C of the Act @ 2%. The Assessing Officer took the view that these reimbursements are liable for tax deduction at source u/s. 194J of the Act @ 10% as against 2% deducted by the assessee u/s. 194C of the Act. Hence, the Assessing Officer, by invoking provisions of section 40(a)(ia) of the Act, disallowed the amount of ₹ 2230.48 lakhs.

9. The learned CIT(A) noticed that an identical issue was adjudicated by him in the assessee's own case in A.Y. 2009-10, wherein the learned CIT(A) has deleted disallowance by following the decision rendered by Hon'ble Kolkata High Court in the case of S.K. Tekriwal (361 ITR 432), wherein it was held that disallowance u/s. 40(a)(ia) of the Act cannot be made in a case of shortfall in the case of tax deduction at source. Accordingly, the learned CIT(A) deleted the disallowance made by the Assessing Officer u/s.40(a)(ia) of the Act in AY 2009-10. Accordingly, by following the order passed by him in AY 2009-10, the Ld CIT(A) deleted the disallowance made by the AO u/s 40(a)(ia) of the Act. Aggrieved by the order passed by the learned CIT(A), the Revenue has filed this appeal before us.

10. We heard the parties on this issue. We noticed that the Revenue had challenged the order passed by the learned CIT(A) in A.Y. 2009-10 by filing appeal before the ITAT. The Tribunal, vide its order dated 11.10.2017 passed in ITA No. 2015/Mum/2013, has confirmed the order passed by the learned CIT(A) with following observations :-

9. We have heard the rival contentions and have gone through the facts and circumstances of the case. We find that the assessee has deducted TDS on payments u/s. 194C of the Act. It is merely an allegation of the Assessing Officer that TDS should have been deducted u/s. 194J of the Act @10%. According to the Assessing Officer this is a short deduction of TDS. The Assessing Officer disallowed the expenses by invoking the provisions of section 40(a)(ia) of the Act. We find that this issue is squarely covered in favour of the assessee by the decision of Hon'ble Calcutta High

Court in the case of S K Tekriwal (supra), wherein the Hon'ble High Court has reproduced the findings of the Tribunal as under:

"... We are of the view that the conditions laid down under section 40(a)(ia) of the Act for making addition is that tax is deductible at source and such tax has not been deducted. If both the conditions are satisfied then such payment can be disallowed under section 40(a)(ia) of the Act but where tax is deducted by the assessee, even under bona fide wrong impression, under wrong provisions of TDS, the provisions of section 40(a)(ia) of the Act cannot be invoked.

Here, in the present case before us, the assessee has deducted tax under section 194C(2) of the Act and not under section 194-1 of the Act and there is no allegation that this TDS is not deposited with the Government account. We are of the view that the provisions of section 4Q(a)(ia) of the Act has two limbs one is where, inter alia, the assessee has to deduct tax and the second where after deducting tax, inter alia, the assessee has to pay into the Government account. There is nothing in the said section to treat, inter alia, the assessee as defaulter where there is a shortfall in deduction. With regard to the shortfall, it cannot be assumed that there is a default as the deduction is not as required by or under the Act but the fact is that this expression, 'on which tax is deductible at source under Chapter XVII-B and such tax has not been deducted or, after deduction has not been paid on or before the due date specified in sub-section (1) of section 139'. This section 4Q(a)(ia) of the Act refers only to the duty to deduct tax and pay to the Government account. If there is any shortfall due to any difference of opinion as to the taxability of any item or the nature of payments falling under various TDS provisions, the assessee can be declared to be an assessee in default under section 201 of the Act and no disallowance can be made by invoking the provisions of section 40(a)(ia) of the Act.

Accordingly, we confirm the order of the Commissioner of Income-tax (Appeals) allowing the claim of the assessee and this issue of the Revenue's appeal is dismissed."

2. We find no substantial question of law is involved in this case and, therefore, we refuse to admit the appeal. Accordingly, the appeal is dismissed.

Similarly, Hon'ble Gujarat High Court in the case of CIT vs. Prayas Engineering Ltd. in Tax appeal No. 1237/2014 dated 17.11.2014, deleted the disallowance on similar facts. Respectfully following the decision of Hon'ble Calcutta High Court in the case of S K Tekriwal (supra) and that of

*Hon'ble Gujarat High Court in the case of Prayas Engineering Ltd (supra),
we confirm the order of the CIT(A) deleting the disallowance.”*

11. We noticed that the Coordinate Bench has followed the decision rendered by Hon'ble Kolkata High Court in the case of S.K. Tekriwal (supra) and also decision rendered by Hon'ble Gujarat High Court in the case of Prayas Engineering Ltd. (Tax Appeal No. 1237/2014 dated 17.11.2014) in this regard. Accordingly, by following the decision rendered by the Coordinate Bench (referred supra), we confirm the order passed by the learned CIT(A) on this issue.

12. The next issue contested by the Revenue relates to addition made for computing profit u/s. 115JB of the Act in respect of expenditure relatable to exempt income. We have noticed earlier that the assessee had disallowed a sum of ₹ 5,90,507/- u/s. 14A of the Act as expenditure relatable to the exempt income. The assessee adopted the same figure for computing profit u/s. 115JB of the Act, wherein it is provided that expenditure incurred by the assessee for earning exempt income has to be added to the net profit for the purpose of arriving at the book profit. We have noticed that the AO has computed the disallowance u/s. 14A as per Rule 8D of the I.T. Rules at ₹ 125.43 lakhs and accordingly added the difference amount of ₹ 119.53 lakhs to the total income of the assessee. The Assessing Officer adopted the very same figure of ₹ 125.43 lakhs as the disallowance to be made u/s. 115JB of the Act. The learned CIT(A), however, restricted the addition to ₹ 5.90 lakhs as made by the assessee as he had deleted the enhancement made by the Assessing Officer u/s. 14A of the Act. The Revenue is aggrieved by the said decision of the learned CIT(A).

13. We have heard the parties on this issue. The Learned AR submitted that the disallowance made by the assessee u/s. 14A of the Act was more than the amount of exempt income. He further submitted that Hon'ble Bombay High Court has held in the case of CIT Vs. Bangalore Finance and Investments Pvt. Ltd. (ITA No. 337 of 2013 dated 10.2.2015) that the amount disallowed

u/s.14A of the Act cannot be added to arrive at the book profit for the purpose of section 115JB of the Act. He submitted that an identical view has been expressed by Hon'ble Delhi Special Bench of ITAT in the case of ACIT Vs. Vireet Investment Pvt. Ltd. (2017) 165 ITD 27. Accordingly, the learned AR submitted that the Ld CIT(A) was justified in deleting the addition made by the AO to compute book profit u/s. 115JB of the Act.

14. The Learned Departmental Representative, on the contrary, placed reliance on the order passed by the Assessing Officer.

15. We noticed that the plea of the Revenue has been decided against the Revenue by Hon'ble Bombay High Court in the case of Bangalore Finance and Investments Pvt. Ltd. (supra). Accordingly, the Assessing Officer was not justified in adopting the disallowance made by him u/s. 14A of the Act for the purpose of computing book profit under section 115JB of the Act. Hence, the learned CIT(A) was justified in deleting the addition so made by the Assessing Officer.

16. Now we shall take up the appeal filed by the revenue for AY 2011-12. The first issue contested by the revenue relates to the disallowance made u/s 14A of the Act. During this year, the assessee declared dividend income of Rs.40.02 lakhs. The assessee disallowed a sum of Rs.60.85 lakhs u/s 14A of the Act. The AO, however, computed the disallowance as per Rule 8D, which worked out to Rs.100.30 lakhs. Accordingly, the AO enhanced the disallowance made u/s 14A of the Act to Rs.100.30 lakhs.

17. The Ld CIT(A) noticed that the own funds available with the assessee was Rs.791 crores and the investments made by the assessee was Rs.16.78 crores. Accordingly he held that no disallowance out of interest expenditure was called for. He further noticed that the disallowance worked out under Rule 8D(2)(iii) out of administrative expenses was less than the amount actually disallowed by the assessee. Accordingly the Ld CIT(A) restricted the

disallowance u/s 14A to Rs.60.85 lakhs, being the amount disallowed by the assessee.

18. We have considered an identical issue in the earlier paragraphs in AY 2010-11 and we have upheld the view taken by the Ld CIT(A). In the year under consideration, the facts are identical. Accordingly we uphold the order passed by Ld CIT(A) on this issue.

19. The next issue contested by the revenue relates to the disallowance made u/s 40(a)(ia) of the Act. As noticed in AY 2010-11, the assessee had deducted tax at source u/s 194C of the Act @ 2% from the amount of reimbursements made to group concerns. The AO took the view that the tax is deductible at source u/s 194J @ 10%. In view of short deduction of tax at source, the AO disallowed the expenditure by invoking the provisions of sec. 40(a)(ia) of the Act. The Ld CIT(A) deleted the disallowance by following his order passed for AY 2009-10, wherein he had followed the decision rendered by Hon'ble Calcutta High Court in the case of S.K.Tekriwal (supra).

20. Identical issue was considered by us in the preceding paragraphs in AY 2010-11 and we have followed the decision rendered by the co-ordinate bench in AY 2009-10, wherein the Tribunal has upheld the view taken by the Ld CIT(A) by following the decision rendered by Hon'ble Calcutta High Court in the case of S.K. Tekriwal (supra). Since there is no change in facts, we do not find any reason to interfere with the order passed by Ld CIT(A) on this issue.

21. The third issue contested by the revenue relates to the addition made to the book profit computed u/s 115JB of the Act in respect of expenditure relatable to exempt income. As in AY 2010-11, the AO adopted the disallowance computed by him u/s 14A of the Act for making addition to net profit for the purpose of computing book profit u/s 115JB of the Act. Since the disallowance enhanced by the AO was deleted by Ld CIT(A), the first appellate authority deleted the addition so made by the AO to the net profit.

22. Identical issue was considered by us in the earlier paragraphs while dealing with the appeal of the revenue filed for AY 2010-11, wherein we have upheld the view taken by Ld CIT(A) for the reasons discussed therein. Accordingly, by following the same, we uphold the order passed by Ld CIT(A) on this issue.

23. We shall now take up the appeals filed by the assessee. The solitary issue urged by the assessee in both the years relate to the rejection of claim for deduction of Service tax liability. The facts relating to the same are discussed in brief. The assessee is liable to pay service tax on the services provided by it. Some of the services are taxable and some of the services are exempt under the Service tax Act. Accordingly the assessee was collecting Service tax on the taxable services rendered by it.

24. The assessee was also paying service tax on some of the services availed by it from other persons. As per the provisions of Service tax Act, the assessee would be eligible to avail "input tax credit" of the Service tax paid by it against the Service tax collected by it, i.e., the assessee would be eligible to deduct the input tax credit from the tax payable by it and accordingly the net amount shall be paid to the credit of the Government. Since the assessee was providing both taxable and exempt services, the eligible input credit amount was bifurcated between both the services in the ratio of value of services. Accordingly the input credit relatable to the taxable service was availed by the assessee by deducting the same against the service tax payable by it. The input credit relatable to the exempt services was charged to the Profit and Loss account, since no credit shall be available to the same.

25. Accordingly, the assessee charged a sum of Rs.184.49 lakhs and Rs.120.51 lakhs respectively in AY 2010-11 and 2011-12 to the Profit and loss account and claimed the same as deduction. It is pertinent to note that the assessee was following "Exclusive method of accounting" for accounting for Service tax, i.e., it did not route the collection and remittance of Service tax

through the Profit and Loss account. Accordingly it was shown as a balance sheet item.

26. The AO took the view that the assessee is following exclusive method of accounting and hence this claim was not routed through the Profit and Loss account. He further observed that the assessee has failed to show as to how the service tax credit on ineligible input services can be transferred to Profit and loss account. The AO also observed that the assessee has failed to furnish the relevant workings. Accordingly he rejected the claim for deduction of Service tax transferred to the Profit and Loss account. The Ld CIT(A) noticed that an identical disallowance was confirmed by him in AY 2009-10 and hence he confirmed the disallowance made by the AO in both the years under consideration.

27. The Ld A.R submitted that the assessee did not contest the decision taken by the Ld CIT(A) on an identical issue in AY 2009-10 in view of the smallness of the amount involved. He submitted that the AO himself has observed in the assessment order that Explanation-II to Cenvat Rules clarifies that credit shall not be allowed on input services used exclusively for provision of exempted services. He further submitted that it is a settled proposition of law that the “Exclusive method” or “inclusive method” followed by the assesseees for accounting for taxes would not have any revenue implication. He submitted that the assessee has no other option but to transfer the input credit relatable to Exempt services to the Profit and Loss account, since it cannot be claimed as credit as per Service tax Rules. The Ld A.R also carried us through the paper book to show the workings furnished by the assessee before the AO, which depicts the segregation of total input credit amount between taxable services and exempt services. He also took us to the Profit and loss account to show that the assessee has duly transferred the Service tax relatable to the exempt services to the Profit and loss account. The Ld A.R also took us through the Service tax returns to show that the assessee has availed input credit relatable to taxable services only.

28. On the contrary, the Ld D.R supported the orders passed by the tax authorities.

29. We have heard rival contentions on this issue and perused the record. There should not be any doubt that the service tax paid by the assessee on the services availed by it, is normally allowed as deductible item of expenditure. As per the provisions of Service tax Rules, the assessee was allowed "input tax credit" in respect of service tax paid by it on the services availed by it. There appears to be no dispute with regard to the fact that the "input tax credit" relating to exempt services are not eligible for input tax credit, since the AO himself has observed so in the assessment order. In the instant case, the assessee has provided both taxable and exempt services. Since the "input tax credit" relating to exempted services are not eligible for input credit, the same has been charged to the Profit and Loss account. We have observed earlier that the service tax paid by the assessee is otherwise eligible for deduction. Hence the input tax credit relating to exempted services is also eligible for deduction, since it cannot be availed as credit by the assessee.

30. We agree with the submission of Ld A.R that the method of accounting Service tax liability, i.e., exclusive method or inclusive method does not have revenue implications. Reference in this regard can be made to the decisions rendered by the Tribunal in the case of Girdhar Fibres P Ltd Vs. ACIT (ITA No.2027/Ahd/2009 dated 12.10.2012) and also in the case of Mohan Spinning Mills vs. ACIT (ITA No.212/Chd/2011 dated 25.04.2012). Hence the observations made by the AO in this regard are not appropriate. In any case, we have noticed that the assessee has duly charged the ineligible input tax credit to the profit and loss account.

31. We have noticed that the Ld CIT(A) has confirmed the disallowance by following his order passed for AY 2009-10, wherein he had confirmed disallowance of identical item on the reasoning that the assessee did not

furnish the relevant details. However, we notice that the assessee has furnished all the relevant details during the years under consideration and the Ld A.R also took us through the same in relation to AY 2010-11 item. The Ld A.R also invited our attention to the Service tax returns filed by the assessee and submitted that the workings given by the assessee also gets authenticated through the Service tax returns, wherein only the eligible input tax credit was carried forward.

32. In view of the above, we notice that the tax authorities have taken adverse view against the assessee without verifying the relevant documents, even though they were furnished before them. Since there is no dispute with regard to the fact that the input tax credit relatable to the exempted services cannot be availed by the assessee, we are of the view that the assessee has rightly claimed the same as deductible expenditure. Accordingly we set aside the orders passed by the Ld CIT(A) on this issue in both the years under consideration and direct the AO to allow them as deduction.

33. In the result, both the appeals of the assessee are allowed and both the appeals of the revenue are dismissed.

Order has been pronounced in the Court on 29.01.2018.

Sd/-
(PAWAN SINGH)
JUDICIAL MEMBER

Sd/-
(B.R.BASKARAN)
ACCOUNTANT MEMBER

Mumbai; Dated : 29/01/2018

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.

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PS

BY ORDER,

Senior Private Secretary
ITAT, Mumbai