

**INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH "G": NEW DELHI**

**BEFORE
SHRI G.S. PANNU, HON'BLE PRESIDENT
AND
MS. ASTHA CHANDRA, JUDICIAL MEMBER**

ITA No. 4691/Del/2018
Asstt. Year : 2014-15

DCIT, Circle-25(2), New Delhi.	Vs.	Trustline Securities Pvt. Ltd., C-647, New Friends Colony, New Delhi - 110 025 PAN AAACK1251G
(Appellant)		(Respondent)

Assessee by:	Shri V.P. Gupta, Advocate Shri Anunav Kumar, Advocate
Department by :	Shri N.K. Chaudhary, CIT (DR)
Date of Hearing	12.04.2022
Date of pronouncement	30.06.2022

ORDER

PER ASTHA CHANDRA, JM

The appeal by the Revenue is directed against the order dated 17.01.2018 of the Ld. Commissioner of Income Tax (Appeals) - 32, New Delhi ("**CIT(A)**") pertaining to the assessment year ("**AY**") 2014-15.

2. The appeal was belatedly filed on 26.06.2018. Pr. CIT Delhi-9 New Delhi made request for condonation of delay. In view of the reasons stated therein the delay in filing appeal was condoned. The Ld. AR had no objection.
3. The Revenue has taken the following grounds :-

- “1. On the facts and in circumstances of the case and in law, the learned CIT(A) has erred in restricting the addition on account of disallowance u/s 14A of the Act read with Rule 8D of the Income-tax Rules from Rs.26,50,909/- to Rs.22,721/-.
2. On the facts and in circumstances of the case and in law, the learned CIT(A) has erred in deleting the addition on account of income from other sources of Rs.24,86,72,622/-.
3. On the facts and in circumstances of the case and in law, the learned CIT(A) has erred in deleting the addition on account of disallowance of Directors’ remuneration of Rs.73,91,440/-.
4. On the facts and in circumstances of the case and in law, the learned CIT(A) has erred in deleting the addition on account of disallowance of lead charges of Rs. 1,94,90,650/-.
5. That the appellant craves, leave or reserving the right to amend modify, alter, add or forego any ground(s) of appeal at any time before or during the hearing of this appeal.”

4. Both the parties have been heard. The Ld. DR supported the order of the Ld. Assessing Officer (**“AO”**). The Ld. AR submitted a paper book containing 265 pages. He also filed written submissions which have been taken on record.

5. The assessee is a company which is a member of National Stock Exchange (**“NSE”**) and also of Bombay Stock Exchange (**“BSE”**). It is engaged in the business of share broking and depository service and brokerage from such services.

6. Ground No. 1 relates to addition of Rs. 26,50,909/- on account of disallowance under section 14A of the Income Tax Act, 1961 (**the “Act”**) read with Rule 8D of the Income Tax Rules, 1962 (**“Rules”**) made by the Ld. AO which has been restricted to Rs. 22,721/- by the Ld. CIT(A).

6.1 The Ld. AO discussed this issue in para 3 of the assessment order. The Ld. AO found that the assessee had made investment in shares which as on 31.03.2014 amounted to Rs. 5,95,53,892/-. The average value of those shares as on 31.03.2014 was Rs. 45,44,163/-. The assessee did not, suo moto, make any disallowance under section 14A of the Act and denied having received any income from investment in shares. No exemption under section 10 of the Act was claimed. It was explained by the assessee that no expenditure, directly or indirectly, has been incurred in respect of exempt income.

6.2 The explanation was not acceptable to the Ld. AO. According to him Rule 8D(2)(iii) has an application even in cases where the assessee is not in receipt of exempted income during the year. But the exempted income may arise in future. The Ld. AO computed the disallowance of Rs. 26,50,909/- under section 14A read with Rule 8D and added the same to the income of the assessee.

6.3 On appeal, the Ld. CIT(A) restricted the impugned disallowance to Rs. 22,721/- by observing and recording his findings in para 5.1c which is reproduced below :-

“5.1c During the appeal hearing, it was reiterated by the AR of the appellant that “...During the year the company had not received any dividend income on investments of Rs.5.95 crores referred above. Only an amount of Rs.87,971/- was received as dividend in respect of shares which had been held by the appellant company as on the record date for the purpose of declaration of dividend by the respective companies as part of its trading stock. Hence, it is submitted that since there has been no dividend income received by the company from investments, no disallowance was called for. It is stated in this regard that as per the decision of Delhi High Court in the case of ACB India Ltd. v. ACIT 374 ITR 108 (Del) and Cheminvest Ltd. v. CIT 378 ITR 33 (Del) only such investments have to be considered for the purpose of disallowance on which income has actually been received during the year. There was no investment on which disallowance is called for...”

*It can therefore be safely inferred from the impugned order that the satisfaction of the AO for disallowance of expenses, in view of the presumed tax-exempt dividend income, u/s 14A of the Act is drawn from the fact that the appellant suo motu did not make any such disallowance. Also, there appears to have been no objective analysis of the appellant's expense in this regard vis-a- vis its accounts. Again, the legislative intent of Section 14A which is to disallow the expenditure in relation to income, which does not form part of total income - requires proper identification rather than disallowing all or proportionate interest and administrative expenses on an ad hoc basis. However, the appellant is in receipt of dividend income of Rs.87,971/-which is otherwise covered u/s 10(34) of the Act. Therefore, I am not in agreement with the appellant's contention that as it had offered the entire dividend income [otherwise not included in the total income u/s 10(34)] it will come out of the ambit of Section 14A r w Rule 8D(2) regarding the disallowance of expenditure related to income that is not includible in the total income of the appellant. My decision is supported by that of the **ITAT Kolkata in Kalyani Barter vs ITO ITA No. 681 and 824 / Kol / 2015**. Further, in my view, the disallowance of expenses u/s 14A would be governed by the decisions of the jurisdictional HC (Delhi HC) and would amount to Rs.22,721/- (0.5% of the average investment wherefrom tax-exempt dividend was received during the year) but restricted to the total tax-exempt income (from dividend) earned in the relevant PY."*

6.4 The Revenue is in appeal before us. The grievance of the Revenue is that the Ld. CIT(A) erred in restricting the impugned addition to Rs. 22,721/- only. The Ld. DR relied on the order of the Ld. AO.

6.5 The Ld. AR submitted that the assessee has been holding the investment in shares of Rs. 5,95,53,892/- in subsidiary companies and in stock exchange companies from earlier years. Neither any investment was made during this year nor any dividend was received on these shares. Investment was made out of own funds as the assessee company was having share capital and reserves of Rs. 31.26 crores as on 31.3.2014. Accordingly, no disallowance was called for.

6.6 We have considered the rival submissions. It is observed that apart from the investment of Rs. 5,95,53,892/- in shares, the assessee being a share broker had certain shares in stock on which dividend income of Rs. 87,971/- was received during the year. The Ld. CIT(A) restricted the disallowance u/s 14A to Rs. 22,721/- being 0.5% of average holding of shares as stock in-trade of Rs. 45,44,163/-. In doing so, the Ld. CIT(A) relied on numerous precedents mentioned in para 5.1d of his order including the judgment of Hon'ble Delhi High Court in ACB India Ltd. vs. ACIT 374 ITR 108 (Delhi).

6.7 We have not found any flaw in the finding of the Ld. CIT(A) which is backed by the judgment (supra) of the jurisdictional High Court. This ground is therefore rejected.

7. Ground No. 2 relates to addition of Rs. 24,86,72,622/- made by the Ld. AO under the head 'Income from other sources' which has been deleted by the Ld. CIT(A).

7.1 The Ld. AO discussed this issue in para 5 of his order. He found that the assessee had taken overdraft facility against pledge of shares from Citi Bank and Kotak Mahendra Bank Ltd.. The outstanding balance as on 31.03.2014 was Rs. 4,04,41,488/- and Rs. 3,72,99,393/- respectively. On perusal of details filed by the banks, the Ld. AO found that the assessee has pledged shares of total value of Rs. 11,70,78,843/- with Citi bank and shares of total value of Rs. 13,64,71,060/- with Kotak Mahendra Bank Ltd. as on 31.03.2014. The value of assessee's own shares in stock as per book was Rs. 48,76,981/- as on 31.03.2014.

7.2 Vide questionnaire dated 07.11.2016 the Ld. AO required the assessee to explain overdraft facility availed from Citi Bank. The assessee furnished explanation vide letter dated 07.11.2016 that the pledge value of shares with Citi Bank as on 31.03.2014 (Rs. 11,70,78,543/-) included assessee's own

shares as well as excess shares of clients. The overdraft facility is provided by the bank on the basis of total value of shares pledged with them.

7.3 The explanation was not acceptable to the Ld. AO. He observed that the shares of clients cannot be pledged for obtaining loans and that confirmation from clients has not been submitted. He, therefore, added the value of difference in shares between book value and pledge value as income of the assessee reducing therefrom value of assessee's own shares which worked out to Rs. 24,86,72,622/- as income from other sources.

7.4 Before the Ld. CIT(A) the assessee contended that it was explained to the Ld. AO that shares of the clients have been pledged for availing margins on behalf of clients. Such clients had authorised the assessee to pledge their shares in order to avail overdraft for depositing margins on their behalf. Three authorisation letters provided by the clients were submitted before the Ld. AO as sample in proof of the above.

7.5 It was pointed out to the Ld. CIT(A) that the assessee has been acting as a leading share broker and also the depository. The transactions of dealing in shares through stock exchange are strictly regulated by SEBI as well as Stock Exchanges. Share broker is required to maintain separate account for each of the clients. There is complete transparency in regard to the transaction of shares undertaken by the assessee on behalf of its clients. The total accounting of the assessee is computerised and is subject to audit and inspection by Stock Exchanges and SEBI. Practice of pledging shares of clients for the purpose of availing margin on their behalf was followed in earlier years also but it was never alleged that shares of the clients belonged to the assessee.

7.6 In para 5.4c of the appellate order, the Ld. CIT(A) recorded the following findings and deleted the impugned addition.

“5.4c From the appellant's submission as well as the arguments put forth by its AR, it is observed that these are borne out from records-copies of

authorization letters of clients as well as audited financials of the appellant and copies of letter from the banks concerned as well as Circular No. 395 of NSE dated 7/04/2004 wherein it is mentioned inter alia, “.In continuation of the said circular, it has now been decided to allow the member – brokers to provide margin trading facility to their clients, in the cash segment, subject to the conditions mentioned in the Circular...

...The broker shall enter into an agreement with his client for providing the margin trading facility, on the lines of the model agreement, enclosed as Annexure 1...

...For the purpose of providing the margin trading facility, a broker may use his own funds or borrow from scheduled commercial banks and / or NBFCs regulated by RBI. A broker shall not be permitted to borrow funds from any other source...

...The broker shall not use the funds of any client for providing the margin trading facility to another client, even if the same is authorized by the client...

...The initial and maintenance margin for the client shall be a minimum of 50% and 40% respectively, to be paid in cash. For this purpose;

(i) “initial margin” would mean the minimum account, calculated as a percentage of the transaction value, to be placed by the client, with the broker, before the actual purchase. The broker may advance the balance amount to meet full settlement obligations.

(ii) “Maintenance margin” would mean the minimum amount, calculated as a percentage of the market value of the securities, calculated with respect to the last trading day’s closing price, to be maintained by the client with the broker...

...The broker shall disclose to the stock exchange/s details on gross exposure including name of the client, Unique Identification Number (UIN) under the SEBI (Central Database of Market Participants) Regulations, 2003, name of the scrip and if the broker has borrowed funds for the purpose of providing margin trading facility, name of the lender and amount borrowed, on or before 12 noon on the following day...”

It is observed from the copies of the covering letters of the appellant produced at the appellate stage that all these information and evidences were submitted at the assessment stage, yet, it is mentioned in the impugned order, "...as per SEBI guidelines shares of client cannot be pledged for obtaining bank finance and company had also not submitted the confirmation from clients whose shares has been pledged for obtaining bank finance..." which appears illogical in the face of the entire discussion above as well as at the assessment stage - shares of clients were pledged with banks for obtaining bank finance for the former's share transactions and not for the appellant per se. Hence, there does not appear to be any conflict with the SEBI guidelines in this regard.

Accordingly, in view of the above and especially the copies of the evidences in this regard put forth by the appellant at both the appellate stage as well as at the assessment stage (as gathered from the appellant's submission as well as from the impugned order itself), the appellant's contention in this regard appears plausible and therefore, the addition made in this regard in the impugned order (Rs.24,86,72,622/-) is deleted."

7.7 The Revenue is aggrieved. The Ld. DR supported the order of the Ld. AO. The Ld. AR reiterated the same contentions raised before the Ld. AO/CIT(A). It was pointed out that the assessee had taken loans on similar basis in earlier as well as later years. Addition had never been made in earlier years. In following year also i.e. AY 2015-16 after considering the assessee's reply, the Ld. AO did not make such an addition. Copy of the assessment order for AY 2015-16 is placed on record.

7.8 We have given careful thought to the submissions of the rival parties. While making the impugned addition the Ld. AO observed that *"it seems that the shares pledged by the assessee company with bank for obtaining working capital facilities were their own shares. In this light I am of the view that the value of shares is an unexplained income of the assessee"*. It is obvious that the addition made by the Ld. AO was not based on any sound legal foundations but on conjecture and surmises. The Ld. CIT(A) quoted extensively from Circular No. 395 of NSE dated 07.04.2004 which allows the

brokers to provide margin trading facility to their clients. For this purpose a broker may use his own funds or borrow from scheduled commercial bank and / or NBFCs, regulated by Reserve Bank of India. The Ld. CIT(A), therefore came to the conclusion that the assessee pledged shares of the clients with banks for obtaining bank finance in order to meet the requirement of depositing margin money by each of the clients as per the regulation of SEBI. We concur with the view of the Ld. CIT(A) and hold that the Ld. AO was not at all justified in taking value of shares pledged as security for taking loans from the banks as undisclosed investment of the assessee. The impugned addition has rightly been deleted by the Ld. CIT(A). We, accordingly reject this ground No. 2 of the Revenue.

8. Ground No. 3 relates to disallowance of directors' remuneration of Rs. 73,91,440/- which has been deleted by the Ld. CIT(A). The Ld. AO discussed this issue in para 7 of the assessment order. He found that the assessee had paid remuneration to the two directors as under :-

1)	Shri Mukesh Kansal	Rs. 60,00,000/-
2)	Shri Vinay Kumar Gupta	Rs. 19,96,000/-

	Total	Rs. 79,96,000/-

According to the Ld. AO the above remuneration paid to the directors was not in accordance with provisions of section 197 of Companies Act, 2013. He therefore calculated allowable remuneration which worked out to Rs. 6,04,560/- and disallowed excess remuneration Rs. 73,91,440/- paid to the directors.

8.1 On appeal, the assessee submitted before the Ld. CIT(A) that the remuneration paid during the year was in consonance with the remuneration paid in earlier years which have been allowed as deduction. It was also submitted that the limits provided under section 198 of the Companies Act

2013 read with Schedule-XIII are not applicable in the case of the assessee in terms of Notification dated 08.12.2017 of the Central Government, a copy of which was submitted.

8.2 The Ld. CIT(A) recorded his findings in para 5.5a and 5.5b of the appellate order and deleted the disallowance for the reasons mentioned therein.

8.3 Being aggrieved the Revenue is before us.

8.4 The Ld. DR defended the order of the Ld. AO whereas the Ld. AR submitted that the assessee had paid remuneration to two directors on same basis in earlier and later years. In subsequent AY 2015-16 no such disallowance has been made by the Ld. AO.

8.5 We have considered the arguments of the parties. We observe that the Ld. CIT(A) has taken note of the fact that the assessee company is a non-government public limited company not listed in the Stock market (shares of the assessee company are not traded). It is because of this reason that the provisions of the Companies Act, 1956/2013 do not apply to the case of the assessee company. We agree with the findings of the Ld. CIT(A) and hold that he has rightly deleted the impugned disallowance. Accordingly ground No. 3 of the Revenue is rejected.

9. The last ground No. 4 relates to disallowance of lead charges of Rs. 1,94,90,650/- made by the Ld. AO which has been deleted by the Ld. CIT(A). The Ld. AO dealt with this issue in para 8 of the assessment order. He found that during the year the assessee had paid above lead charges to 270 parties. According to him, the assessee company could not make payment on account of lead charges/commission to its business associates/authorized persons as per SEBI guidelines. Since the assessee did not submit agreement /confirmation and debit note in this regard, the Ld. AO made the impugned disallowance.

9.1 On appeal, the Ld. CIT(A) deleted the disallowance by observing in para 5.6a as under :-

“5.6a It is gathered from the appellant’s submissions that para 7.13.1 of the Model Bye Laws prescribed by SEBI for operations by stock brokers states, inter alia, “A trading member may share brokerage with a sub-broker, remisier or employee in his own exclusive employment subject to the provisions contained in Bye-law 7.5.2 and further subject to such terms of brokerage as agreed upon in writing by way of an agreement. He may similarly share brokerage with any other person introducing a client provided such person -

7.13.1.1 is not one for or with whom trading members are forbidden to do business under the Rules, Bye- laws and Regulations of the Exchange;

7.13.1.2 is not a sub-broker or remisier of any other trading member of the Exchange;

7.13.1.3 is not an employee of any other trading member;

7.13.1.4 does not advertise in the public, press or in any other manner that he is acting as a broker;

7.13.1.5 does not pass contracts in this own name...”

Thus, it is clear that the appellant’s contention, borne out from records as well as in accordance with the extant law - the trading member (appellant) may share the brokerage with any other person introducing a client, albeit meeting all the parameters prescribed under para 7.13 of the Model Bye laws. Further, it is gathered from the submissions as well as from the arguments put forth by the AR of the appellant that despite providing requisite details - list of clients to whom lead charges were made in the relevant PY - details were also provided at the appellate stage along with their individual payments, TDS made and their PAN as well as list of parties (received > Rs.1 lac) along with list of clients for whom payments were made to the business associates / authorized persons.

*Finally, the final decision to incur business expenses lies on the businessman and the AO cannot dictate decisions as held by the Hon’ble apex court in **SA***

Builders Limited vs. CIT (supra). Accordingly, the disallowance of payment lead charges in the impugned order (Rs. 1,94,90,650/-) is **deleted.**”

9.2 Aggrieved the Revenue is in appeal before us.

9.3 We have heard the submissions of the parties. The Ld. DR supported the order of the Ld. AO and Ld. AR submitted that the assessee in order to develop its clientele had entered into agreement with certain persons who were introducing new clients and had been sharing brokerage income with them. The arrangement was as per guidelines of SEBI. No similar disallowance was made in earlier years. Even in the following AY 2015-16 no such disallowance has been made.

9.4 On consideration of the rival submissions, we are of the opinion that the disallowance made by the Ld. AO does not rest on sound footing as despite requisite details filed by the assesses before him, he made the impugned disallowance which is not sustainable. Agreeing with the findings of the Ld. CIT(A) which is backed by the judgment of the Hon'ble Supreme Court in SA Builders Ltd. vs. CIT 288 ITR 1 (SC), we reject ground No. 4 of the Revenue as well.

10. In the result, the appeal of the Revenue is dismissed.

Order pronounced in the open court on 30th June, 2022.

Sd/-

**(G. S. PANNU)
PRESIDENT**

sd/-

**(ASTHA CHANDRA)
JUDICIAL MEMBER**

Dated: 30/06/2022

Veena

Copy forwarded to -

1. Applicant
2. Respondent
3. CIT

4. CIT (A)
5. DR:ITAT

ASSISTANT REGISTRAR
ITAT, New Delhi

Date of dictation	
Date on which the typed draft is placed before the dictating Member	
Date on which the typed draft is placed before the Other Member	
Date on which the approved draft comes to the Sr. PS/PS	
Date on which the fair order is placed before the Dictating Member for pronouncement	
Date on which the fair order comes back to the Sr. PS/PS	
Date on which the final order is uploaded on the website of ITAT	
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Date on which the file goes to the Head Clerk	
The date on which the file goes to the Assistant Registrar for signature on the order	
Date of dispatch of the Order	