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Court : Income Tax Appellate Tribunal ITAT Mumbai

Decided On : Mar-29-2007

Judge : S K Yadav, V Gupta

Appellant : ito

Respondent : Kamu Metals (P) Ltd.

Judgement :
1. This appeal filed by the Revenue is directed against the order of the learned CIT(A). We have heard both the parties and perused the material on record.

2. In this appeal the Revenue has raised the following effective grounds: 1. On the facts and in the circumstances of the case and in law, the learned CIT(A) erred in not accepting the finding of the assessing officer that since the assessee is holding units by way of investment, it cannot be said to be in business.

2. On the facts and circumstances of the case and in law, the learned CIT(A) erred in holding that the assessee is engaged in business of investment and the professional fees incurred thereon is allowable as business expenditure.

3. The facts, in brief, are that original assessment was completed under Section 143(3) vide order dated 21-11-1999 wherein, the returned income was accepted. Subsequently, case was re-opened under Section 148. In the course of reassessment proceedings, the assessing officer noted that the assessee had shown Rs. 16,95,257 in the credit side of the P&L Account on the sale of units of

J.M. Mutual Fund and this Memorandum of Understanding was shown as Short Term Capital Gain (STCG) while computing taxable income. The assessing officer also noted that the assessee had claimed business expenditure on account of professional charges at Rs. 10,75,000, audit fees Rs. 10,000, bank charges of Rs. 79 and these business expenses were treated as business loss and had been set off against the STCG. The assessing officer asked the assessee to furnish the details of business transactions carried on by the assessee-company during the financial years relatable to assessment years 1997-98 and 1998-99. The assessee, in response to this requirement of the assessing officer, filed acknowledgement of return of income. The assessing officer again asked the assessee that why the professional charges should not be disallowed as the assessee did not carry out any business activity during the year. The assessee replied that the assessee was engaged in the business of holding of investments and dealing in investment as one of the business activity, hence, these professional charges were allowable as expenses. The assessing officer also analysed the nature of activities carried on by the assessee in subsequent assessment years 1998-99, 1999-2000, 2000-01 and 2001-02 and found that in all these years the assessee either earned dividend or sold investments resulting into long-term capital loss. The assessing officer also noted that the assessee during this period neither purchased any commodity nor sold any commodity and these assets were shown as investment in the balance sheet. The Assessing A Officer also analysed the object Clause of Memorandum of Association in reference to Clause No. 80 of other objects which authorised the assessee to carry on business of share broker etc. and, accordingly held that assessee had not carried out any of these activities. Finally, the assessing officer held that these activities could not be categorised as business activities and therefore, these expenses were not allowable under Section 37 of the Income Tax Act, 1961. The assessing officer, thereafter, held that the professional fees was also not allowable under Section 48 of the Act. Aggrieved by this, the assessee carried the matter into appeal before the learned CIT(A).

4. In the appellate proceedings, the assessee relied on Clause 85 of Memorandum of Association which authorized the assessee to carry on the business of investments. The assessee also drew support from Section 40A(8). Section

2(5B)(ii) of the Interest Tax Act, 1974 and decision of the Division Bench of the Tribunal in the case of Barkha Investment & C Trading Co. in ITA No. 1129 Ahmedabad, dated 27-2-1992 to contend that the activity carried on by the assessee could be classified as an activity of business of holding investments. The assessee also contended that the fact income arising from investment was not assessed under the head 'Profits and gains of business or profession' was not relevant as the income in essence was of the nature of business income.

The assessee also referred to the Scheme of Act regarding taxation of income and submitted that classification of income under various heads was only for the purpose of computing net income of the assessee and nature of income was to be decided on commercial principles. For this purpose, he relied on the decision of the Hon'ble Supreme Court in the case of CIT v. Cocanada Radhaswami Bank Ltd. . The assessee also referred to the requirements of part two of Schedule VI to the Companies Act, 1956 requiring the companies to disclose income or loss in respect of investment in the profit and loss account which could be inferred as recognition of investment activity as a "business activity". The learned CIT(A), accepted the contentions of the assessee and directed the assessing officer to allow professional fees incurred in connection with the business of investment as business expenditure.

The relevant findings of the learned CIT(A) are extracted as below: I have considered the submissions of the appellant and also perused the impugned order of assessment. The assessing officer has disallowed the F professional fees only on the ground that the appellant is holding the shares by way of investments and the same cannot be business of the appellant. The appellant has been in the business of investment activity and finance and the said activities are being carried out in organized manner with the said purpose of earning profit. It is not essential that the stock-in-trade can only be the medium for carrying out the business. The appellant company was incorporated in the year 1996 and as per the Clause 85 of the Memorandum of Association the appellant is permitted to carry on the business of investment company and to undertake all such activities which go with the investment business. The appellant has also raised funds for acquiring shares and securities from time to time. The term 'business' as defined in the IT Act is very wide and covers all activities which are carried out in an organized manner. The fact that the shares have been shown as investment in the accounts does not decide the issue under consideration. The investment are made with a view to earn return thereon and make profits. The same can be in the form of dividend, interest, profit on investments etc. The Hon'ble ITAT, Ahmedabad Tribunal Bench in the case of Barkha Investment & Trading Co. (P) Ltd. has also recognised the acquisition of shares, stocks, bonds etc. as a business of an investment company. The Income Tax Act, 1974 has also incorporated a definition of "Financial Company" which includes an investment company which carries on as its principal business, acquisition of shares, stocks etc. Thus all the acts have accepted business of investment like any other business.

5. Both the sides reiterated their respective stands on the issue of whether there could be a business of holding of investments or not. The decisions relied on by both the sides included the decision of Hon'ble Apex Court, Hon'ble High Courts and that of the Tribunal. Revenue also referred to various sections of the Act and contended that as on date there was no concept of business of holding of investments. The learned Departmental Representative also contended that since the income earned by the assessee was taxable under the head 'Capital gains', hence, Section 28 was not applicable and, therefore, other sections falling under the head 'Profits and gains of business or profession' were also not applicable. The learned Departmental Representative also contended that, at the most, the professional expenses could be considered as capital costs incurred for the purpose of acquiring shares/units being capital assets.

6. The learned authorised representative contended that the assessing officer had accepted the business losses to the tune of Rs. 10,079, hence, the assessing officer had himself accepted the activity carried on by the assessee as one of business. It was also contended by him that the disallowance of professional fee was not made by the assessing officer on the ground that it was a capital expenditure, hence, this plea could not be taken at this stage. The learned authorised representative also contended that once it was held that assessee was engaged in the business of holding of investments, the other consequences were natural i.e. the expenditure incurred in connection with the business activity of the

assessee was allowable as business expenditure. The learned authorised representative also contended that irrespective of taxability of income under specific head these expenses were allowable as business expenses.

7. We have considered the submissions made by both the sides, material on record and orders of authorities below. We have also considered all the decisions cited by respective parties though we have not referred these decisions in our order because decisions are mainly related to the aspect whether there could be a business of holding of investments or not. The reason for not referring to these decisions in this manner is that because in our opinion the issue is required to be adjudicated upon if it is assumed or established that there can be a business of holding of investments, whether in that situation, the assessee can get deduction under the head 'Profits and gains of business or profession' where the income arising to the assessee out of these activities is assessable either under the head 'Capital gain or income from other sources'. Before examining this legal issue we consider it pertinent to state that in the year under consideration as well as in the subsequent 3-4 years, the assessee has invested in the mutual funds/shares which have yielded only dividend and/or resulted in capital gain/losses.

Thus, in the facts of the case, the existing income or the possible income is assessable under the head 'Capital gain or income from other sources'. In our opinion, the question is very simple and can be answered through having a plain look at the scheme of the Act where incomes of various natures have to be computed under specific heads according to commercial nature/ character thereof unless a specific provision is made otherwise for e.g., dividend income on shares held as stock-in-trade, under the provisions of present Act, is to be computed under the head 'Income from other sources', whereas prior to 1955, the same was taxed either as profits or gains of business or under the head 'Income from other sources' depending upon the nature of shares i.e., whether held as stock-in-trade or investment. Similarly, even if the assessee is engaged in the business of constructing commercial properties and lets out such property on hire, income from letting of such would invariably, be computed under the head 'Income from house property'. Having stated so, the next question which arises for our consideration is that it is the income which is to be computed under a specific head and not the allowance /deduction of expenses alone to be given ie. if there exists an income, may be a loss or such income may ultimately be less than the amount chargeable to tax and if this be the only source of income then, the assessee would be entitled to deduction of expenses thereon. Further, if there exist no income but there is always a possibility of an income being generated which may be assessable under that head even then the deductions can be given provided assessee satisfies other conditions e.g., the assessec must carry on the business during the year. Thus, the existence of an income either in the present or in the future under that head is pre-supposed.

In this background, now we have to look the scheme of computation of income under the head 'Profits and gains of business or profession'.

Section 28 applies only in respect of business or profession, profits or gains of which are assessable under that head under the Income-tax Act. Section 28 is a charging section which provides for income of various natures which can be treated as profits or gains of business or profession. Section 29 of the Act states that in computing the income referred to in Section 28 deduction under Sections 30 to 43D would be given. A bare perusal of the language employed in Section 29 makes it clear that deduction under Sections 30 to 43 D are allowable only A with respect to income which is chargeable under Section 28. Hence, if an income is not so chargeable deductions under Sections 30 to 43D shall not be given. Since, in the year under consideration, there exist receipts or gross income of the nature which is not chargeable under Section 28, hence, no deduction under Sections 30 to 43D can be allowed. To further elaborate, allowability of expenditure has got an implied nexus with the income or entity ie. during the course of business an expenditure is B always incurred with a view to earn some income or to protect the business assets or for administrative purposes, therefore, such expenditure is relatable directly or indirectly to the nature of that income. The list of expenses spelt out under any head of the Act reflect this position, even the term "for the purpose of business" though certainly wider than the term "for the purpose of earning of income or profit but it inherently imbibes the theory of relatability of expenditure with the income. Hence the deductibility of any expenditure is necessarily based upon the existence of income or possibility of an income under that head.

Accordingly, professional charges paid by the assessee are not allowable as business expenditure since these have been incurred in connection with the deployment of funds resulting into income chargeable under the head 'Capital gains'.

8. Further, we do not find any substance in the contention of the assessee that for the purpose of deduction taxability of income under any other head is not relevant because head of income are mutually exclusive and scheme of the Act, that the income falling under each one of them should be separately computed under those head, is clear.

Further, commercial character of income can be considered for any purpose such as set off of loss under Section 72, but it cannot be so for the purpose of computation of income under a specific head.

Admittedly, commercial character of the income in the present case is that of capital gain and it has been so treated by the assessee itself in the books of account and by off ering the same as E capital gain as well hence, in the present case the head of chargeability of this income is capital gain on all counts, therefore, the assessee can get only such deductions which are enumerated under Section 48 of the Act.

Further, we do not find any substance in the contention of the assessee to allow professional charges also merely because audit fee and bank charges have been treated as business loss for the reasons that two wrongs cannot make a right and these expenses, being required to be incurred for maintenance of corporate structure, cannot be treated at par professional charges for the reasons stated herein before. We may also add that in the case of Cocanada Radhaswami Bank Ltd. (supra), the Honble Apex Court was seized with the question of set off of loss against interest on securities earned by the assessee on securities held as trading assets. In these circumstances, the Hon'ble Court held that interest on such securities was in the nature of income from business on commercial principles, hence, loss was liable to be set off against such interest. There is no dispute about this proposition and we have also stated so herefi ioefore, however, for the purpose of computation of income under a particular A head, the ratio in this decision does not render any assistance to the cause of the assessee.

Further, even at the cost of repetition, we may state again that even the commercial character of income in the present case is of capital gain and even the dividend income is of the nature of return on investment in capital asset.

9. In view of the above discussion, we are of the considered view that the assessee is not eligible for deduction of professional fees under the head 'Profit and gain of business or profession' and consequently, it is also not eligible for set off of the same as business loss against short-term capital gain. Accordingly, we reverse the finding of the CIT(A). Thus, this ground of the revenue stands allowed.