IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED: 08.03.2019

CORAM

THE HON'BLE DR.JUSTICE VINEET KOTHARI
AND
THE HON'BLE MR.JUSTICE C.V.KARTHIKEYAN

Tax Case Appeal No. 1389 of 2009

M/s. Patterson & Co Pvt. Limited.,
Vanguard House
48, Second Line Beach
Chennai - 600 001. Appellant / Respondent

Vs.

The Deputy Commissioner of Income Tax
Company Circle V(1)
Chennai. Respondent//Appellant

Tax Case Appeal filed under Section 260A of the Income Tax Act, 1961 against the order of the Income Tax Appellate Tribunal, Madras 'D' Bench, Chennai, dated 31.07.2009 made in ITA No.2110/mds/ 2008.

against the order passed by the commissioner of Income Tax (Appeals) -V, Chennai dated 19/03/2008 made in ITA.392/2005-06 for the Assessment Year 2003-04 and against the Assistant Commissioner of Income Tax Company Circle V (i) Chennai dated 30/1/2005 made in PAN /GIR.No.AAACP 5364P 51018-P for the Assessment Year 2003-04.

For Appellant : M/s.J.Balachander
& K.Kavitha

For Respondent : Mr. T.Ravikumar
Senior Standing Counsel

J U D G M E N T
(Delivered by DR.VINEET KOTHARI, J)

The Assessee has filed this Appeal raising the following questions of law arising from the order of the learned Tribunal 31.07.2009 allowing Revenue's Appeal and setting aside the order of the learned CIT (Appeal) for the Assessment Year 2003-2004.

2. The questions of law on which the present Appeal was admitted by the Co-ordinate Bench on 21.12.2009 are quoted below for ready reference:-

> "i. Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in law in disallowing the sum of Rs.9 lakhs paid to its sister concern as advisory fees on the ground that there are no documentary evidence produced when in the nature of trade such documentary evidence is not possible to be maintained as all institutions are conveyed by telephonic messages?
>
> ii. Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in law in holding that the competency of the recipient of advisory fees is not relevant for making the disallowance of a legitimate expenditure which is not disproved by the Revenue Authorities?
>
> (iii) Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in law in holding that the right person to be assessed is the appellant even though the recipient has offered a sum of Rs. 9 lakhs as its income and has paid necessary tax for the same? And
>
> (iv) Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was right in law in holding that the disallowance of expenditure made is not because of lack of genuineness of the transaction but only on the score that it is paid to the sister concern.?"

3. The finding of the learned Tribunal with regard to the disallowance of Rs.9 lakhs paid by the Assessee Company to its sister concern M/s.Patterson & Co., (partnership firm) as Research and Advisory fees are as follows:-

"3.1 On this issue, the Assessing Officer found that assessee company has claimed payment of advisory fees of Rs.9 lakhs to M/s. Patterson & Co., Pvt., Ltd. The said amount was paid as research and advisory fees towards business procurement, research and advisory services. In this regard, a copy of the Agreement was also filed. The Assessing Officer found that the assessee company has paid this amount to a firm in which Mr.Amarnath, Director of assessee company has substantial interest. The Assessing Officer was of the opinion that payment has been made to a person as specified in Section 40A (2)(b)(v). The assessee was not in a position to produce any documentary evidence regarding the services rendered by M/s. Patterson & Co. Pvt. Limited. Under such circumstances, the Assessing Officer disallowed the amount involved under Section 37 holding that it was not made for the purpose of business. The Assessing Officer also held that the payment has been made to a person covered under Section 40A(2)(b)(v) which was clearly unreasonable.

3.2 Upon assessee's appeal, the learned Commissioner of Income Tax (Appeals) held that M/s. Patterson & Co. Limited., had a long standing and rich experience with clients in share trading business. Hence, it has the competence to offer advice. The payment was under an agreement. There was also not any intention to avoid tax. Hence, he deleted the addition made by the Assessing Officer.

3.3 Against this order Revenue is in appeal before us. It has been contended on behalf of the Revenue that the learned Commissioner of Income Tax (Appeals) failed to appreciate that the assessee neither before him nor before the Assessing Officer had furnished documents, records or accounts maintained by the assessee company to establish that services had, indeed, been rendered by the sister concern.

3.4 The learned counsel of the assessee on the other hand submitted that the advisory services were orally provided. It was also claimed that on the fees received, M/s. Patterson & Co. Pvt., Limited., has paid tax and so there is no element of tax avoidance.

3.5 We have carefully considered the submissions. It remains an admitted fact that assessee has not produced any evidence whatsoever to establish that services had indeed been rendered by the sister concern. The competence of the payee is not relevant in establishing the fact to actual extent. The claim that such services were rendered orally can only be termed as a self-serving statement. Under such circumstances, when the impugned expenditure is not allowable in the hands of the assessee, the claim that proper tax has been paid by the payee company and hence the payment should be allowed, cannot be accepted.

3.6 Hon'ble Apex Court in the case of ITO vs. C.H.Atchaiah 218 ITR 239 (SC) has held that it is the duty of the Assessing Officer to assess the right person only. Accordingly, we set aside the order of the learned Commissioner of Income Tax (Appeals) and restore that of Assessing Officer on this issue."

4. The learned counsel for the Assessee has vehemently submitted before us that the learned CIT (Appeal) was perfectly justified in allowing the said advisory fees in the hands of the Assessee Company as an allowable deduction by finding that there was an Agreement between the Assessee Company and its sister concern M/s.Patterson & Co., Pvt. Limited., for providing advice for business procurement and research and Advisory service to the Assessee Company, which was engaged in the business of share broking and therefore, merely because such advices were received orally, such professional fees paid to the said partnership firm, the sister concern M/s.Patterson & Co., could not have been disallowed by the Assessing Authority under Section 40A(2)(b) of the Act, which empowers the Assessing Authority to

disallow an expenditure, if the same is incurred by way of payment to a relative of the Assessee or in case of Company to any Director or partnership Firm or member of Association of the family.

5. The purpose of disallowance under the said provision is to avoid diversion of income from the hands of the Assessee to its related persons.

6. The findings of the learned CIT (Appeal) in favour of the Assessee are quoted below for ready reference:-

> "6. The next issue relates to research and advisory fee paid by the assessee company to a sister concern, Patterson and Company towards business procurement and research and advisory services rendered by them. The relevant facts are that after April, 2001 the capital market was in doldrums and the assessee company, in order to survive in its business of stock broking, opted to avail the expertise of its sister concern, Patterson & Company, which had been in the market much longer. Through an agreement entered into with Patterson & Company, the assessee company agreed to pay 50% of brokerage earnings of the assessee company subject to a maximum limit of Rs. 9 lakhs towards services of procurement of business and market advise to be rendered by the sister concern. As the 50% of the brokerage earnings for the period under consideration amounted to Rs.16,10,467/-, the maximum permissible amount of Rs. 9 lakhs was paid to the sister concern Patterson & Company for the professional services rendered by them.
>
> 7. The Assessing Officer noted that Shri M.Amarnath, a Director in the assessee company, had substantial interest in the firm Patterson & Company to which the payment of Rs.9 lakhs was made. Thus, the payment was made by the assessee company to a related person as specified in Section 40A (2)(b)(v) of the Income Tax Act. The Assessing Officer further required the assessee company that services had, indeed, been rendered by the sister concern. The assessee stated before the Assessing Officer

that no separate documents or books of accounts were maintained to evidence this claim and the payment of research and advisory fee was solely based on the copy of agreement filed with the Assessing Officer. In these facts the Assessing Officer came to the conclusion that such payments had not been made for the purposes of the business of the assessee company and that the payment made to a related party were clearly unreasonable and the Assessing Officer proceeded to disallow such claim in the assessment order.

8. It is a fact that stock broking is a highly competitive industry which also experiences periodical downturns in business. There being restrictions to advertising and sales promotion, the only way to generate and expand business is through appointment of advisors and sub-brokers. It is also not in dispute that the sister concern was a long established firm in the stock broking business with a rich experience in the field and had the requisite competence to render advice to the assessee company. From the records available, it is seen that several clients with larger transactions such as L.I.C and Central Bank of India and other high net worth individuals during the period under consideration carried on stock market transactions through the assessee company on the recommendation of the firm Patterson & Company. Client registration application forms evidencing such diversion of business from the firm Patterson & Company to the assessee company are available on record. Again, given the nature of the business of stock broking, market advice and recommendations required to advise the clients of the assessee company would be provided by the firm Patterson & Company through telephone on a continuous basis and the assessee cannot be blamed for not maintaining records of such telephonic advice received from the firm Patterson & Company."

7. Per contra, the learned counsel for the Revenue supported the impugned order.

8. We are of the considered opinion that as a matter of fact, no substantial questions of law arise in the present Appeal filed by the Assessee. The findings of the learned Tribunal even though upon reversal of the order passed by learned CIT (Appeals) in the present case cannot be said to be perverse in any manner and they remain findings on facts. Therefore, it cannot be contended that merely because there was an Agreement between the Assessee Company and the related party or the partnership firm, the Research and Advisory fees made by the Company to the partnership firm, in which one of the Directors Mr.Amarnath had a substantial interest, ought to be allowed wholly or partly as a business expenditure. The mere fact that the same person, Mr.M.Amarnath who had substantial interest in the partnership firm, was the person to whom Research and Advisory fees was paid by the Assessee Company was also the Director in the Assessee Company itself and could have rendered such advisory services to the Assessee Company in the best business interest of Assessee Company even pro bono in which he himself was the Director. Therefore, naturally a doubt could arise in the minds of the Assessing Authority about the genuineness of the payment made to the partnership firm, a related party in which the same person had substantial interest. It will naturally therefore depend upon the facts and circumstances of the case, whether disallowance under Section 40A(2)(ab) of the Act could be made or not.

9. With respect to establishing the disallowance under Section 40(A)(2)(ab) of the Act, in our opinion, the learned Tribunal on the basis of materials available before it, cannot be said to have committed any perversity in making such disallowance even though resulting in the reversal of the order passed by the First Appellate Authority viz., CIT (Appeals). The Tribunal being the second and higher tier of the Appellate Forums viz., higher than the CIT (Appeal), naturally has the same and wider powers of the lower Appellate Authority and therefore reversal by the final fact find body ie., the Tribunal in all such cases need not be and cannot be declared to be perverse. The scope of Section 260-A of the Act is limited and only the substantial questions of law can be entertained and answered by the High Court under Section 260-A of the Act.

10. We do not find any such substantial questions of law arising in the present case. Equally we do not find any merit in the contentions raised on behalf of the appellant / Assessee on the facts of the case and therefore, the present appeal of the Assessee deserves to be dismissed and the same is

accordingly dismissed. The questions framed above are answered against the Assessee and in favour of the Revenue. No costs.

Sd/-

Assistant Registrar (CCC)

//True Copy//

Sub Assistant Registrar

Vsg

TO

1.INcome Tax Appellate Tribunal,
Madras D Bench, Chennai.

2.The Deputy Commissioner of Income Tax,
Company Circle V (1),
Chennai.

3.The Commissioner of Income Tax Appeals V,
Chennai 600 034.

4.The Assistant commissioner of Income Tax
Company Circle V (1), Chennai.

+1cc to Mr.T.Ravi Kumar, Advocate, S.R.No. 22733

Tax Case Appeal No. 1389 of 2009

SR(CO)
GN(12/04/2019)