

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

**BEFORE SHRI B.R. BASKARAN, ACCOUNTANT MEMBER AND
SHRI PAWAN SINGH, JUDICIAL MEMBER**

**ITA No.1588/M/2011
Assessment Year: 2007-08**

M/s. Directi Internet Solutions Pvt. Ltd., 102, Osia Friendship, Gaothan Lane No.4, Off: J.P. Road, Opp. Ram Mandir, Andheri West, Mumbai – 400 058 PAN: AACCG4058M	Vs.	Income Tax Officer, Circle-9(1)(3), Mumbai
(Appellant)		(Respondent)

Assessee by : Shri Firoze Andhyarujina, A.R.
Revenue by : Shri B.S. Bist, D.R.

Date of Hearing : 28.07.2016
Date of Pronouncement : 14.09.2016

ORDER

Per B.R. Baskaran, Accountant Member:

The appeal filed by the assessee is directed against the order dated 12.01.11 passed by Ld. Commissioner of Income Tax (Appeals) [hereinafter referred to as the CIT(A)]-19, Mumbai relevant to assessment year 2007-08.

2. The grounds of appeal by the assessee give rise to the following issues:
 1. Treatment of interest income of Rs.23.94 lakhs.
 2. Disallowance made under section 14A of the Act.
 3. Apportionment of common expenditure between STPI and non STPI units.
3. The assessee company is engaged in information technology, computer software and IT enabled services, more particularly in web development and the website services such as domain name registration, web using services etc.

The assessee is eligible for deduction under section 10A of the Act in respect of profits derived from STPI unit.

4. The first issue relates to treatment of interest income of Rs.23.94 lakhs received by the assessee from inter-corporate loan given by it. During the year under consideration, the assessee had taken a loan of Rs.3 crores from Karnataka Bank Ltd. for the purpose of purchasing an office premise. Since the payment towards the purchase of office premises was not required to be made immediately, the assessee advanced the above said amount of Rs.3 crores to M/s. Acme Housing India Pvt. Ltd., at interest rate of 18% per annum. The assessee had borrowed the money from Karnataka Bank Ltd., at the rate of 11% per annum. The interest income of Rs.23.94 lakhs received on the inter corporate loan so given was offered by the assessee as its business income. The Assessing Officer (hereinafter referred to as the AO), however, treated the same as income from other sources and the same was also confirmed by the Ld. CIT(A).

5. The Ld. A.R. submitted that the assessee has given the loan of Rs.3 crores to M/s. Acme Housing India Pvt. Ltd. in the ordinary course of its business and hence the interest income should be assessed under the head 'Business'. Alternatively, the Ld. A.R. submitted that the assessee has paid a sum of Rs.15,38,239/- to Karnataka Bank Ltd. for availing the loan of Rs.3 crores and the same should be set off against the interest income of Rs.23.94 lakhs and the balance amount of Rs.8.56 lakhs of loan may be considered as income under the head 'Income from other sources'.

6. On the contrary, the Ld. D.R. submitted that giving of inter corporate loan is not the business activity of the assessee and hence the Ld. CIT(A) was justified in confirming the assessment of interest income under the head 'Income from other sources'.

7. We have heard the rival contentions and perused the record. The assessee has furnished the copies of bank account and also ledger account copy of M/s. Acme Housing India Pvt. Ltd. A perusal of the bank account shows that the term loan amount of Rs.3 crores has been credited to the account of the assessee on 29.09.06. On the very same day the assessee has transferred Rs.1.50 crores to M/s. Acme Housing India Pvt. Ltd. and on 03.10.06 another amount of Rs.1.50 crores has been transferred. Thus, we notice that the term loan of Rs.3 crores has been fully utilized for giving loan to M/s. Acme Housing India Pvt. Ltd. We have noticed earlier that the business of the assessee is related to information technology and IT enabled services. Hence, we do not find merit in the submissions of the assessee that the above said loan of Rs.3 crores was given in the ordinary course of carrying on business. The assessee itself has submitted that the loan was given to M/s. Acme Housing India Pvt. Ltd., since the term loan proceeds were not immediately required. The Ld D.R has also pointed out that the lending of money is not part of business activities carried on by the assessee. Hence the interest income cannot be considered to be the business income of the assessee, since the interest corporate loan was given out of the term loan availed by the assessee for purchasing a house property, i.e., the loan has been given as the term loan was not required to be used immediately. Under these set of facts, we are of the view that the tax authorities are justified in assessing the interest income of Rs.23.94 lakhs as income of the assessee under the head 'Income from other sources.

8. With regard to alternative contention of the assessee that the interest paid on term loan should be set off against the interest income, we are of the view that the same requires examination at the end of the AO, since the alternative contention has not been examined by him. It is not clear from the record as to how the interest expenditure relating to the term loan was treated in the books

of account and how it was allowed by the AO. If the alternative claim of the assessee is accepted, then the corresponding adjustments are required to be made in other heads also. Accordingly we restore the alternative contention of the assessee to the file of the AO with a direction to examine the same afresh after affording adequate opportunity of being heard to the assessee and take appropriate decision in accordance with law.

9. The next issue relates to disallowance made under section 14A of the Act. The assessee has declared dividend income of Rs.2,03,820/- and claimed the same as exempt. The AO computed the disallowance under section 14A of the Act at Rs.5.70 lakhs by applying the provisions of Rule 8D of IT Rules. The Ld. CIT(A) however restricted the addition to Rs.50,000/-, since the Hon'ble High Court has held that the provisions of Rule 8D shall not apply to the year under consideration.

10. We have heard the rival contentions and perused the record. The Hon'ble Jurisdictional Bombay High Court has held in the case of "Godrej & Boyce Manufacturing Co. Ltd. Vs. DCIT" [(2010) 328 ITR 81 (Bom)] that the provisions of Rule 8D shall be applicable from assessment year 2008-09 onwards and for the earlier years the disallowance should be made on reasonable basis. The contention of the assessee is that the interest free funds available with was more than the investments made and hence, no disallowance is required out of interest expenditure. We find merit in the said contentions. Hence the disallowance, if any, is required to be made only in respect of administrative expenses incurred in the dividend income. Accordingly, we are of the view that the disallowance of Rs.50,000/- confirmed by Ld. CIT(A) is also on the higher side. Accordingly, we modify the order of Ld. CIT(A) and direct the AO to restrict the disallowance to 2% of the dividend income as held by Hon'ble Bombay High Court in the case of "Godrej Agrovet Ltd. vs. DCIT" 232 ITR 97 (Bom.).

11. The next issue relates to allocation of common expenses between STPI and non-STPI units. The AO noticed that the assessee has followed different criteria for apportioning the common expenses between STPI and non-STPI units. The AO was not convinced with the same and accordingly allocated the expenses in the ratio of sales. The Ld. CIT(A) also confirmed the same.

12. The Ld. A.R. contended that the assessee has followed a scientific basis for allocating various expenses and hence the same should be upheld. On the contrary, the Ld. D.R. submitted that the assessee has not given any justification for adopting different criteria for allocating various expenses. He further submitted that the Ld CIT(A) has also highlighted the flaw in the method adopted by the assessee.

13. We have heard the rival contentions on this issue and perused the record. We notice that the Ld. CIT(A) has upheld the action of the AO with the following observation:

"8. I have considered the said submissions. There is no dispute as regards allocation of direct expense since they are charged to the respective units. The dispute is with regard to allocation of indirect expenses. The A.O. has taken the view that such indirect expenditure is to be allocated in proportion of sales of the eligible unit to that of total sales. In this regard, I have called for the specific details of allocation as carried out by the appellant. As per the details submitted by the appellant, it is seen that no uniform standards or parameters has been applied by the appellant company for the purpose of allocation. In fact, different variables have been used for the purpose of allocation. For instance, it is seen that in respect of expenses debited under the head "Administrative Expenses", canteen expenses are apportioned between the domestic and STPI unit on the basis of employee ratio, courier charges in the ratio of Domain Name Registration Expenses, Electricity charges on the basis of employee ratio, insurance on the basis of employee ratio, traveling on the basis of employee ratio. As regards Personal expenses the allocation is on the basis of employee ratio between the domestic and the STPI Unit. The selling and distribution expenses are seen allocated either on the basis of employee ratio or on the basis of Domain Name Registration Expenses. The foreign travel is seen allocated on the basis of Domain Name Registration expenses ratio between the domestic and STP Unit. As regard foreign exchange fluctuation it is seen that the allocation has been done on the basis of Domain Name registration Expenses/Server Ratio/Employee Ratio/Digital Certification

Sales Ratio. Thus, it is seen that different variables have been used for the purpose of allocation of common expenses. On a consideration of the standards used it cannot be stated that there is any scientific basis for the same. For example it is seen that electricity expenses has been allocated on the basis of employee ratio rather than space. Hence, I am unable to agree with the contention of the appellant that it is based on prudence and past practice that allocation as carried out by him has been made. On the other hand the A.O. has undertaken a pro-rata approach which appears to be most reasonable considering the fact that the variable as adopted by the appellant company is based on subjective judgment, rather than any rational or scientific method amenable to any transparent yardstick of measurement. In the circumstances, the best course open is to allocate the common expenses pro-rata on the basis of turnover, which is a standardized and reasonable method as carried out by the A.O. The action of the A.O. in this regard is confirmed."

14. We notice that the assessee has not given the justification for adopting different criteria for apportioning the expenses. Hence, we are of the view that the Ld. CIT(A) was justified in rejecting the claim of the assessee that the criteria adopted by it was scientific, particularly in the case of electricity expenses, i.e., the allocation has been done on the basis of employee ratio instead of floor space used.

15. At the same time, we are of the view that the allocation of Canteen expenses on the basis of employee ratio, Courier charges on the basis of Domain Name registration expenses ratio, Personal expenses on the basis of employee ratio cannot be found fault with. However, the allocation of electricity expenses, Insurance expenses, Travelling expenses, Selling & distribution expenses on the basis of employee ratio does not appear to be scientific. Similarly, the allocation of foreign exchange fluctuation on the basis of domain registration etc. does not appear to be scientific. The foreign exchange fluctuation can be linked to specific items and how it is not understandable as to how the same was treated as common expenses. At the same time, adoption of sales ratio as the basis for allocation of expenses across the board also does not appear to be correct. Accordingly we are of the view that this issue also requires fresh examination at the end of the AO.

Accordingly, we set aside the order passed by Ld CIT(A) on this issue and restore the same to the file of the AO with the direction to examine this issue afresh after affording adequate opportunity to the assessee to present more suitable method of allocation and take appropriate decision in accordance with the law.

16. In the result, the appeal filed by the assessee is treated as partly allowed for statistical purposes.

Order pronounced in the open court on 14.09.2016.

**Sd/-
(Pawan Singh)
JUDICIAL MEMBER**

**Sd/-
(B.R. Baskaran)
ACCOUNTANT MEMBER**

Mumbai, Dated: 14.09.2016.

* Kishore, Sr. P.S.

Copy to: The Appellant
The Respondent
The CIT, Concerned, Mumbai
The CIT (A) Concerned, Mumbai
The DR Concerned Bench

//True Copy//

By Order

Dy/Asstt. Registrar, ITAT, Mumbai.