IN THE INCOME TAX APPELLATE TRIBUNAL

"A" BENCH, MUMBAI

BEFORE SHRI I.P.BANSAL, JUDICIAL MEMBER AND SHRI SANJAY ARORA, ACCOUNTANT MEMBER

ITA No.8596 /Mum/2010
(Assessment year 2007-2008)

Kaprecon Sleeper Works. Pvt. Ltd. 303, Elphinstone House, 17, Marzban Road, Fort, Mumbai **PAN: AAACK1814C**	Vs.	The Dy. Commissioner of Income Tax-1(2) Mumbai.
Appellant		**Respondent**

Appellant by: Shri Damodar Kabra
Respondent by: Shir Manoj Kumar

Date of Hearing: 17-06-2013
Date of Pronouncement: 17-06-2013

ORDER

PER I.P.BANSAL, JM

This appeal is filed by the assessee, it is directed against the order passed by CIT (A) dated 14th October, 2010 for assessment year 2007-2008.

2. Grounds of appeal has raised by the assessee as under.

> *"1. The Ld. Commissioner of Income Tax (Appeals)-2 Mumbai, hereinafter referred to as " the CIT(Appeals), erred in holding that, the disallowance of medical expenses incurred during the year of Rs. 43,76,229/- on one of the directors of the appellant company, as made by the Assessing Officer, is justified.*
>
> *The appellant submit that, on the facts and in the circumstances of their case, the medical expenses incurred by the appellant company during the year on one of its full-time directors are allowable business expenditure.*
>
> *2. The CIT(Appeals) erred in upholding the disallowance of administrative expenses as made by the Assessing Officer u/s 14A of the I-T Act at Rs. 49,750/- on the principles contained in Rule 8D of the IT Rules.*
>
> *The appellants submit that, on the facts and in the circumstances of their case, no disallowance u/s 14A of the IT Act is called for.*

Without prejudice to the above, the appellants submit that, Rule 8D of the IT Rules is not applicable and consequently, the principles contained in Rule 8D are not applicable for the year under appeal.

Without prejudice to the above, it is submitted that, the disallowance of Rs. 49,750/- towards administrative expenses as per section 14A of the IT Act are highly excessive and unreasonable.

3. The CIT(Appeals) erred in enhancing the income of the appellants by Rs. 17,255/- towards disallowance of interest as per the formula contained in Rule 8D of the IT Rules.

The appellants submit that, on the facts and in the circumstances of their case, no disallowance out of interest is required to be made as contemplated under Rule 8D of the IT Rules.

Without prejudice to the above, he appellants submit that, on the facts and in the circumstances of their case, Rule 8D of the IT Rules is not applicable and consequently, even the principles contained therein cannot be applied for the year under appeal.

3. **Ground No. 1**:- It is the common contention of both the parties that this issue is covered by the earlier of the Tribunal and the facts and circumstances regulating the grounds are identical. The issue relates to allowability or otherwise of the medical expenses of a Director. Similar expenditure was incurred by the assessee in Assessment Year 2006-07 to the tune of Rs. 1,33,42,405 which was disallowed and disallowances was upheld by the Learned CIT (A). The order of the CIT was upheld by the Tribunal. While deciding the same issue in the present appeal, Ld. CIT(A) has referred to the order passed by him in respect of assessment year 2006-07. The Tribunal has upheld this disallowance vide order dated 3rd February, 2012 passed in ITA No. 525/Mum/2010. For better understanding of the facts and decision taken by Tribunal, the relevant portion of the order passed by the Tribunal for the Assessment Year 2006-07 is reproduced below.

Ground No. 2 is relating to the disallowance of Rs. 1,33,42,405/-.

9. During the course of assessment proceedings the AO had observed that the assessee company had debited an amount of Rs. 1,33,42,405/- on account of medical expenses incurred for one of the Directors of the Company. The AO asked the assessee to submit the details in respect of medical expenses like copies of medical bills, RBI permission, ledger a/c extract, copy of ITR of concerned director,namely, Shri A.G. Patil. The assessee filed the said required details, on perusal of which the Assessee noticed that the medical expenses were incurred towards liver transplant surgery of Shri AG Patil and total amount of Rs. 1,33,42,405/- was paid in India rupees towards the said surgical operation including the travel expenses. The AO further noticed that the said amount was debited to the books of M/s Raghavendra Prestress Product Pvt. Ltd., on behalf of the assessee company. The AO asked the assesee to submit the explanation in respect of aforesaid expenses for allowing it as *regular business. The assessee company submitted as under:- "Shri AG Patil, a director of the company was serving the company right from its incorporation till his death in March 2007 as can be seen from the accounts. He was looking after the entire business of the company on a meager remuneration of Rs. 50,000/- to Rs. 60,000/- per month. After taking into account all the f acts of the case, the board of the company took a decision to bear expenses of medical treatment of Shri AG Patil, one of the directors is wholly and exclusively incurred for the purpose of business of the assessee company and are accordingly allowable as business expenditure. Further, AR of the assessee submitted that, in view of decision of Bombay High Court in the case of Mehoob Productions Pvt. Ltd., Vs. CIT, 106 ITR 758, medical expenses are allowed if it is incurred for the director."*

10. After considering the said submissions of the assessee, the AO had observed that the expenditure incurred by the assessee towards liver transplantation of Mr. A.G. Pail, director was a general expenditure and if same was to be allowed, it had to satisfy the conditions stipulated in section 37(1) of the Act. After considering the conditions in section 37(1), the AO observed that the nexus between the expenditure claimed and the business, in connection with which expenditure had been incurred, has to be established before the assessee gets entitled to deduction u/s 37(1) of the Act, on the ground of commercial expediency and compelling necessity. He further observed that in assessee's case, terms of director's employment did not make his medical treatment to be borne by the company and the director did not suffer illness directly due to any hazardous assignment given by the company or by way of accident met which attending to any company work. Therefore, the AO held that the expenditure incurred by the assessee company for its director's treatment could not be called as business income. In so far as the case law relied upon by the assessee in the case of Mehbook Production Pvt. Ltd. (supra), the AO noted that in the said case the director had fallen sick while on tour undertaken for business of company and thereof the company had to bear cost of his treatment while in assessee's case under consideration, the director fell ill in normal course and the assessee decided to send him abroad for treatment. Therefore, the AO observed that the facts of the case in Mehaboob Production Pvt. Ltd. (supra) are materially different and the ratio could not apply in the assessee's case. He, therefore, made an addition of Rs. 1,33,42,405/- incurred by the assessee towards medical treatment for one of its director Mr. AG Patil, in the hands of the assessee company. Aggrieved by the order of the AO, the assessee carried the matter in appeal before the CIT(A).

11. Before the CIT(A), the learned AR of the assessee was argued that the Director on whose surgery expenditure had been incurred by the assessee company was in employment of the assessee company since its incorporation till he expired in March, 2007 and the director was looking after the entire business of the assessee company at a meager remuneration of Rs. 50,000/- to Rs. 60,000/- per month. He, therefore, submitted that the Board of directors had taken a conscious decision to bear the medical expenses o the director and the same was claimed as incurred for the purpose of business. After considering the submissions of the assessee, the CIT(A) confirmed the addition made by the AO by holding as under:-

> *"9. I have perused the f acts of the case. As f ar as the contention that expenditure has been incurred under contractual obligation is concerned, I am not satisf ied. Firstly AO in the order of assessment has categorically mentioned that the expenditure has not been incurred under any contractual obligation. That means that AO was categorically given impression that there was no contractual obligation upon appellant company to incur an expenditure under consideration. In this back ground now appellant is*

> *producing a letter about the terms of employment of the Director. This letter is an af ter thought because otherwise it ought to have been placed before AO. I also f ind that the letter under consideration has reference to Board Meeting. If the contents of the letter were really genuine, they should have formed an integral part of minutes of the Board meeting o the appellant company. Nothing of this kind has been brought to my knowledge. A resolution of the Board granting medical benefits to the Director would have been on a altogether different footing. In such a situation the additional evidence placed before me cannot be accepted and I decline to take cognizance of this letter for deciding the issue under consideration.*
>
> *10. What remains to be decided for the issue under consideration is as to whether the expenditure is allowable as being wholly and exclusively for the purpose of the business of appellant company. I f ind that AO has given very detailed reasons as to why the expenditure under consideration cannot be said to be wholly and exclusively for business of appellant company. I also f ind that there are various decisions on medical expenses of corporate entity incurred on directors and in these decisions it has been consistently held that these expenses are allowable as integral part of contractual terms of agreement with the Director which, in the present f acts of the case does not appear to be so. Consequently, it is held that the disallowance made by the AO is perfectly justif ied. The ground of appeal is rejected."*

12. Still aggrieved, the assessee is in appeal before us.

13. Before us, the learned counsel for the assessee submitted that the assessee company had incurred the expenditure towards liver transplantation of one if it's founder director of the company, who worked till his death and, therefore, the Board has taken a conscious decision to bear the expenditure incurred for the surgical operation. He, therefore, contended that the said expenditure should be allowed as business expenditure within section 36(iii) or section 37(1) of the Act. It is submitted that the assessee has produced a letter before the CIT(A) with regard to approval of the Board to incur the said expenditure to the Director and the same was rejected by the CIT(A) without giving any proper reason. In this connection, the learned counsel referred to pages 98 & 99 of the paper book and submitted that at page 98 terms and conditions of the appointment were mentioned vide letter dated 9 t h April, 2003. Therefore, the assessee is under obligation to bear the medical expenses to the director and accordingly the same has to be allowed as business expenditure. It is further submitted that the page 99 of paper book is extract of the minutes of the meeting of the Board to establish that the expenditure for the director has been approved by the Board. In support of assessee's case, the learned counsel for the assessee has relied upon the following case laws:-

1. Bharat Bijlee Ltd. Vs. DCIT, 71 ITD 412 (Mum.)

2. Ajay Singh Deol Vs. JCIT, 91 ITD 196 (Mum.)

3. CIT Vs. Nainital Bank Ltd., 62 ITR 638(SC)

4. M/s Khambare Chemicals (I) Pvt. Ltd. Vs. ITO, for AY 2005-06 in ITA No. 2394/Mum/2009 dt. 18/11/2011.

5. Sarna International Ltd. Vs. ACIT, 308 ITR 202(AT)(Del.)

14. On the other hand, the learned DR strongly relied upon the orders of the authorities below and submitted that the additional evidence filed by the assessee before the CIT(A) dt. 94/04/2003 was an after thought for simple reason that when AO asked the assessee to explain the reasons for incurring the medical expenses to the director, the assessee explained that the said expenditure was incurred that since the director was working since company's inception to till death, the board has taken a conscious decision to incur the said expenditure. Therefore, the additional evidence filed by the assessee before the CIT(A) at pages 98 & 99, which are terms and conditions of employment and extract of minutes of meeting was rejected by the CIT(A) and confirmed the addition made by the AO

Therefore, the DR submitted that the order of the CIT(A) may be upheld.

15. We have heard both the parties, perused the record and gone through the orders of the authorities below as well as the decisions cited. The issue to be adjudicated before us is whether the expenditure incurred by the assessee company to its one of directors for liver transplantation is a business expenditure or not?. During the course of assessment proceedings, the AO asked the assesee to produce all the details in respect of the said expenditure, and also specifically asked to produce the evidence that the assessee was under any employment obligation. In response to the said queries, the assessee submitted all the details in respect of the said expenditure. With regard to the terms and conditions of employment, it was submitted before the AO that the director was working since the company's inception to till death, therefore, the company has taken a conscious decision to incur the said expenditure to the director. Before the CIT(A) the assessee has produced a letter dated 09/04/2003 wherein one of the condition of the employment is to provide medical expenses including hospitalization for the self and family of the directors of the company has to be paid/borne by the company. The said letter was rejected by the CIT(A) on the ground that if at all the terms and conditions of employment provides, the same letter could have been produced before the AO and he was of the view that the letter is an after thought when the AO rejected the claim of the assessee on the ground that the terms and conditions of employment does not provide to incur the medical expenses on behalf of the director, therefore, the said letter was made/created later on to produce before the CIT(A). We fully agree with the findings of the CIT(A) for the simple reason that when the AO specifically asked the assesee to produce any resolution passed by the Board of the company with regard to terms and conditions of employment that reimbursement of medical expenses to the directors, the assessee did not produce any such letter before the AO. In fact, it was submitted that the Board has taken a conscious decision to extend the help to the director because he was the founder director since its inception to till his death with a meagre salary of 50000 to 60000 salary per month. Therefore, it can be safely concluded that when the AO posed specific question to the assessee that any employment terms and conditions provide for incurring the said medical expenditure to the director, the assessee could not produce any documentary evidence and, therefore, the letter dated 09/04/2003 filed before the CIT(A) was an after thought to support its claim, which was rejected by the CIT(A) submitted by the assessee as additional evidence. In so far as the case laws relied upon the assessee are distinguishable on facts and the same are not of any help to the case of the assessee as the cases were decided by taking into consideration of the facts in each case. After careful consideration of the facts of the case, we conclude that the expenditure incurred by the assessee for the purpose of liver transplantation surgery to the director Mr. AG Patil is not incurred on the ground of commercial expediency and compelling necessity and the assessee has not substantiated its claim by way of material evidence. Therefore, we uphold the order of the CIT(A) in confirming the addition of Rs. 1,33,42,405/- made by the AO on account *of expenditure incurred by the assessee towards liver transplantation to the director of the company. Thus, this ground of appeal of the assessee is dismissed."*

4. It may also be mentioned here that according to papers submitted before us Hon'ble High Court vide its orders dated 9th March, 2013 and 3rd April 2013 has admitted the question of law on this issue for AY 2006-2007 as under.

"Whether, on the facts and in the circumstances of the case and in law, the Tribunal erred in disallowing the medical expenditure incurred on one of the Directors of Rs.1,33,42,405/- as not an allowable expenditure ?"

In this view of the situation as it was fairly admitted by Ld AR that there is no difference on the facts & circumstances relating to this issue as compared to the facts & circumstances for Assessment Year 2006-07, respectfully following the aforementioned order of Tribunal in assessee's own case for Assessment Year 2006-2007 we dismiss the ground.

5. **Ground No. 2**:- Learned CIT(A) has upheld disallowance u/s 14A with reference to Rule 8D of the of the Income Tax Rule 1962. However, Rule- 8D has not been held to be applicable by Hon'ble Bombay High Court in the case of Godrej Boyce Manufacturing Company Ltd. Vs. DCIT 328 ITR 81(Bom), wherein it has been held that as Rule 8D has been inserted with effect from 24th March, 2008 and the same will be applicable from assessment year 2008-2009. However, at the same time it is held that even if Rule 8D is not applicable for assessment year earlier to Assessment Year 2008-2009, then also the AO was duty bound to compute the disallowance by applying a reasonable method having regard to the facts and in the circumstances of the case. Therefore, after hearing the both parties, we consider it just and proper to restore this issue to the file AO with a direction to recompute disallowance in accordance with aforementioned decision of Hon'ble Bombay High Court in the case of Godrej and Boyce Manufacturing Private Ltd. Vs. DCIT (Supra). We direct accordingly. Needless to observe that AO will provide to the assessee a reasonable opportunity of hearing in this regard. This ground is allowed for statistical purpose.

6. In the result, the appeal is **partly allowed for statistical purpose** in the manner aforesaid.

Order Pronounced in the open court on the 17th day of June,2013.

Sd/- Sd/-

(SANJAY ARORA) (I.P.BANSAL)
ACCOUNTANT MEMBER JUDICIAL MEMBER

Mumbai, dated 17th June 2013.
Pramod

<u>Copy to:</u>

1. *The Appellant*
2. *The Respondent*
3. *The concerned CIT(A)*
4. *The concerned CIT*
5. *The DR, " A " Bench, ITAT, Mumbai*

By Order

Assistant Registrar
Income Tax Appellate Tribunal,
Mumbai Benches, MUMBAI