

IN THE INCOME TAX APPELLATE TRIBUNAL  
'C' BENCH , Mumbai

**BEFORE K.P.T.THANGAL (VP) & DR.O.K.NARAYANAN (AM)**

ITA No. 7888/M/03  
Assessment Year – 2000-01

PAN No. AADPK6785F

Shri Sudhir Kapadia  
102, Sibylle, Worli Hill Road,  
Worli, Mumbai – 400 018

V/s.

Income Tax Officer,  
Ward 11(3) (3),  
4<sup>th</sup> floor, Aaykar Bhavan,  
Mumbai – 400 020

(Appellant)

(Respondent)

Appellant by : Shri A.V. Sonde  
Respondent by : Smt. Aparna Teredesai

**ORDER**

**Per DR O.K. NARAYANAN, AM**

This appeal is filed by the assessee. The relevant assessment year is 2000-01. The appeal is directed against the order of CIT(A) XI, Mumbai dated 10/10/03 and arises out of the assessment completed u/s 143(3) of Income Tax Act,1961.

2. The assessee is a Chartered Accountant by profession and a partner of a CA firm. In the computation of his income, the assessee has claimed a deduction of Rs.3,95,500/- incurred mainly for motor car expenses and relating to depreciation. The Assessing Officer found that the above expenditure cannot be claimed as deduction against share income of the assessee from the partnership firm. This is because the share income from the partnership firm is exempt from tax u/s 10(2A). The Assessing Officer therefore applied

the provisions of law containing 14A and disallowed the proportionate amount of Rs.3,09,792/-, attributable to share income from the firm. In first appeal this disallowance has been confirmed. Secondly the assessee has claimed a loss of Rs.78,410/- on account of cancellation of sale agreement dated 18/12/99, for the purchase of a flat at Nasik. The claim of the assessee was that the proposal to purchase the flat was in the nature of an adventure in trade and therefore the loss arising out of such proposal needs to be treated as revenue expenditure. This was disallowed by Assessing Authority on the ground that the transaction does not have any relation with the profession carried on by the assessee and therefore the loss as claimed by the assessee could not be allowed as deduction. This was confirmed in first appeal. Therefore the second appeal before us.

3. We heard Shri Arvind V. Sonde, Id. Counsel appearing for the assessee and Smt. Aparna Teredesai, Id. SR DR appearing for the Revenue.

4. ITAT, Mumbai bench 'J' in the case of Sudhir Dattaram Patil Vs DCIT 2 SOT 678 (Mum) has considered the question of taxing the expenditure while computing income of a partner against salary received by the partner from the firm. The Tribunal held that the salary from the firm in which the assessee is a partner is in the nature of business income u/s 28 (v) and therefore, interest paid by the partner on money borrowed for contributing capital has to be allowed as deduction in the hands of the assessee. In respect of the nature of the share in the profits of a firm, in the hands of the partner, the Supreme Court has considered the issue in the case of CIT, Madras Vs. R.M. Chidambaram Pillai 106 ITR 292. The court was examining the nature of share of profits received by a partner. The court held that a firm is not a legal person even though it has some attributes of

personality. In Income Tax law a firm is a unit of assessment, by special provisions, but is not a full person. Since a contract of employment requires two distinct persons, the employer and the employee, there cannot be a contract of service, in strict law, between a firm and one of its partners. Payment of salary to a partner represents a special share of the profits. Salary paid to a partner retains the same character of the income of the firm. ITAT, Mumbai bench 'H' in the case of ACIT Vs. Rustom J. Gagrati, has considered the very same issue for the assessment year 97-98 in its order dated 31/12/04 in ITA No.3860/M/00. There also the Tribunal has held in favour of assessee that deduction is permissible under law.

5. When we examine the issue in the light of the above judgement and decisions, we find that the claim made by the assessee is acceptable in law. The Supreme Court in the case of CIT, Madras Vs. R.M. Chidambaram Pillai has held that salary paid to a partner retains the same character as income of the firm. This leads us to the next step: i.e. the share of profits received by the partner from the firm retains the same character of the income of the firm: i.e. the share income retains the character of business income. The said business income is exempt from the levy of tax only in the hands of the assessee; but it is taxable in the hands of the firm. The assessee partner gets its share of profit from the firm after firm has been subjected to tax in its hands. Therefore, it is not possible to hold the view that the share income in the hands of a partner is all together tax free; on the other hand the share is tax suffered income in the hands of the firm. Therefore, Sec 14A is not applicable in that case. The share income of the firm is exempt from the tax u/s 10(2A), not in the absolute sense. It is only to avoid double taxation; once in the hands of the firm and secondly in the hands of the partner. Therefore we find that the provisions of

section 14A would not apply to the assessee / partner and it is not necessary for the Assessing Authority to disallow the proportionate expenditure from the claim of the assessee . Therefore, the disallowance of Rs.3,09,792/- is deleted and the Assessing Officer is directed to allow Rs.3,95,500/- claimed by the assessee. This finding is fortified by the fact that the assessee partner is not allowed to claim any conveyance expenditure from the firm as provided in the partnership deed [ please refer to statement of facts filed before the CIT(A).]

6. Regarding disallowance of Rs. 78,410/-, we do not find any merit in the contention raised by the assessee. The assessee has suffered the loss on cancellation of the agreement to purchase the flat at Nasik. The assessee being a Chartered Accountant. in practice, no other business activity, regular or random could be conceived in his needs. Disallowance of loss of Rs.78,410/- is therefore confirmed.

7. In result this appeal filed by the assessee is partly allowed.

Order pronounced in the Open Court at the time of hearing.

Sd/-  
(K.P.T.THANGAL)  
Vice – President

Sd/-  
(DR.O.K.NARAYANAN)  
Accountant Member

Mumbai, Dated : 26<sup>th</sup> February, 2007

NN

*Copy to :*

1. *The Appellant*
2. *The Respondent*
3. *The CIT-concerned*
4. *The CIT(A)-concerned*
5. *The DR 'C' Bench*

*True Copy*

*By Order*

*Asstt. Registrar, I.T.A.T, Mumbai*

IN THE INCOME TAX APPELLATE TRIBUNAL  
H-BENCH, MUMBAI

BEFORE SHRI J. SUDHAKAR REDDY, AM  
AND  
SMT. P. MADHAVI DEVI, JM

I.T.A. No.993/Mum/2007  
(Assessment year 2003-04)

Hitesh D Gajaria  
BSR & Co, KPMG House  
Kamala Mills Compound  
Senapati Bapat Marg  
Lower Parel, Mumbai-13  
PAN : AAFPG7109K  
(Appellant)

vs ACIT 11(2)  
Mumbai

(Respondent)

Appellant by : Shri Arvind Sonde  
Respondent by : Shri Mayank Priyadarshi

ORDER

Per Shri J Sudhakar Reddy, AM

This is an appeal filed by the assessee and is directed against the order of the CIT(A)-XI, Mumbai dated 15-11-2006 for the assessment year 2003-04.

2. In ground No.1 the assessee agitates the confirmation of disallowance of Rs.1,16,752 out of expenses of Rs.3,90,268 claimed by the assessee against his business income being remuneration from a partnership firm in which he was a partner. The facts are that the assessee claimed an expenditure of Rs.3,90,268 from his total income. The assessing officer finding that the assessee has claimed deduction of the share income from partnership firm which is exempt u/s 10(2A), apportioned the expenditure claimed by the assessee in view of provisions of section 14A of the Act which resulted in reduction of the claim of expenditure by Rs.1,16,752. On appeal, the first appellate authority agreed with the findings of the assessing officer and confirmed the disallowance. Further aggrieved, the assessee is in appeal.

3. We have heard Shri Arvind Sonde, the learned counsel for the assessee and Shri Mayank Priyadarshi, the learned departmental representative.

4. We have considered the arguments of the parties and perused the material placed before us. We find that similar issue was considered by "C" Bench of the Mumbai Tribunal vide order dated 26<sup>th</sup> February, 2007 in the case of Shri Sudhir Kapadia vs ITO in ITA No.7888/M/03 and the Tribunal dealt with the issue in the following manner:

"4. ITAT, Mumbai bench 'J' in the case of Sudhir Dattaram Patil Vs DCIT 2 SOT 678 (Mum) has considered the question of taxing the expenditure while computing income of a partner against salary received by the partner from the firm. The Tribunal held that the salary from the firm in which the assessee is a partner is in the nature of business income u/s 28(v) and therefore, interest paid by the partner on money borrowed for contributing capital has to be allowed as deduction in the hands of the assessee. In respect of the nature of the share in the profits of a firm, in the hands of the partner, the Supreme Court has considered the issue in the case of CIT, Madras Vs. R.M. Chidambaram Pillai 106 ITR 292. the court was examining the nature of share of profits received by a partner. The court held that a firm is not a legal person even though it has some attributes of personality. In Income Tax law a firm is a unit of assessment, by special provisions, but is not a full person. Since a contract of employment requires two distinct persons, the employer and the employee, there cannot be a contract of service, in strict law, between a firm and one of its partners. Payment of salary to a partner represents a special share of the profits. Salary paid to a partner retains the same character of the income of the firm. ITAT, Mumbai bench 'H' in the case of ACIT Vs. Rustom J. Gagrati, has considered the very same issue for the assessment year 97-98 in its order dated 31/12/04 in ITA No.3860/M/00. there also the Tribunal has held in favour of assessee that deduction is permissible under law.

5. When we examine the issue in the light of the above judgment and decisions, we find that the claim made by the assessee is acceptable in law. The supreme court in the case of CIT, Madras Vs. R.M. Chidambaram Pillai has held that salary paid to a partner retains the same character as income of the firm. This leads us to the next step: i.e. the share of profits received by the partner from the firm retains the same character of the income of

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We find that the issue is also covered in favour of the assessee by the decision of "E" Bench of the Tribunal in the case of Shri Bharat S Raut in ITA No.9212/Mum/2004 and CO No. 212/Mum/2005 vide order dated 25<sup>th</sup> June, 2008. Thus, respectfully following the precedent, we delete the disallowance.

5. In the result, the appeal filed by the assessee is allowed.
6. Order pronounced on this 14<sup>th</sup> November, 2008.

Sd/-  
(Smt. P. Madhavi Devi)  
Judicial Member  
Mumbai, Dt: 14<sup>th</sup> November, 2008

sd/-  
(J. Sudhakar Reddy)  
Accountant Member

pk/-  
Copy to:  
1. the appellant  
2. the respondent  
3. the CIT  
4. the CIT(A)  
5. the DR, H-Bench  
(True copy)

By order

Asstt.Registrar, ITAT, Mumbai Benches