IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH "I" MUMBAI

BEFORE SHRI SAKTIJIT DEY (JUDICIAL MEMBER) AND
SHRI N.K. PRADHAN (ACCOUNTANT MEMBER)

ITA No. 6950/MUM/2016
Assessment Year: 2010-11

Mateen Pyarali Dholkia 90, Gr. Floor, Hill Road, Opp. Vijaya Bank Bandra (W), Mumbai-400050.	Vs.	DCIT-19(3) Aayakar Bhavan, M.K. Road, Mumbai-400020.
PAN No. ABAPD1241K **Appellant**		**Respondent**

Assessee by : Mr. Anil Thakrar, AR
Revenue by : Mr. Saurabh Kumar Rai, DR

Date of Hearing : 17/05/2018
Date of pronouncement : 30/05/2018

ORDER

PER N.K. PRADHAN, AM

This is an appeal filed by the assessee. The relevant assessment year is 2010-11. The appeal is directed against the order of the Commissioner of Income Tax (Appeals)-33, Mumbai [in short 'CIT(A)'] and arises out of the assessment completed u/s 143(3) of the Income Tax Act 1961, (the 'Act').

2. The ground of appeal filed by the assessee reads as under:

The Ld. CIT(A)-33 erred in confirming the disallowance of Rs.26,04,585/- on account of PMS Fees under the Head of Capital Gains of Rs.97,87,309/-on sale of shares.

3. Briefly stated, the facts of the case are that the assessee/appellant filed his return of income for the assessment year (AY) 2010-11 on 29.07.2010 declaring total income of Rs.1,05,92,370/-. The assessee, a partner in M/s Goldfield Mercantile Company, derived income by way of capital gains on sale of shares and mutual funds and also received interest income from Bank and other parties.

During the course of assessment proceedings, the Assessing Officer (AO) found that the assessee had earned capital gains amounting to Rs.97,87,309/- on sale of shares under a Portfolio Management Scheme (PMS) with Surefin Consultants Pvt. Ltd. on sale of shares against which he had paid consultancy and operating expenses of Rs.46,93,398/- to SCPL. Also out of total expenses of Rs.46,93,398/-, the assessee had claimed Rs.26,04,585/- against capital gains earned through PMS.

The AO was not convinced with the above claim of the assessee on the ground that as per the mandate of section 48 of the Act, income chargeable under the head "Capital Gains" is computed after allowing deductions viz. (i) expenditure incurred wholly and exclusively in connection with such transfer, (ii) cost of the acquisition of the asset and (iii) cost of any improvement thereto from full value of consideration received or accruing as a result of the transfer of the capital asset.

The AO held that the PMS fees paid by the assessee neither falls under the category of transfer fees, nor cost of acquisition/improvement. Therefore, he disallowed the assessee's claim of Rs.26,04,585/- on account of PMS fees against capital gains.

4. Aggrieved by the order of the AO the assessee filed an appeal before the Ld. CIT(A). Reliance was placed by the assessee on the decision in *DCIT v. KRA Holding & Trading Pvt. Ltd*. [ITA No. 240 & 356 (PN) of 2011] while distinguishing the order in *Homi K. Bhabha v. ITO (International Taxation)* [2011] 48 SOT 165 and *Devendra Kothari* (2011) 13 taxmann.com 15 (Mumbai). While deciding the appeal, the Ld. CIT(A) followed the decision in *Devendra Kothari* (supra) and *Homi K. Bhabha* (supra). Also the Ld. CIT(A) observed that in the decision in *Homi K. Bhabha* (supra), the Tribunal has elaborated two important aspects in para 6 and 8 which he extracted at para 6.4 of his order dated 08.08.2016 as produced below:

> "(1) the decision of the Pune Bench in KRA Holding & Trading Pvt. Ltd. (supra) was primarily based on the judgment of the Hon'ble Bombay High Court in the case of CIT v. Smt. Shakuntala Kantilal (1991) 190 ITR 56 (Bom), which had been subsequently held to be not a good law by the Hon'ble Bombay High Court in CIT v. Roshanbabu Mohammed Hussein Merchant (2005) 275 ITR 231 (Bom). The later judgment overruling the earlier judgment was not brought to the notice of the Hon'ble Pune Bench.
>
> (2) on referring to various clauses of the PMS agreements regarding consideration payable to the Portfolio Manager, it is observed by the Hon'ble Tribunal that it was at half per cent of the net asset value (market value of assets inclusive of all securities and cash balances) under management at the beginning of each quarter and further the portfolio managers were entitled to a return based fee calculated @ 20% per annum of the profits in excess of 15% of the profits after deducting all the expenses. The sum and substance of the AR's submission was that such fees paid by the assessee has direct relation with the income arising from the transfer of shares."

4.1 The Ld. CIT(A), thereby following the decision in *Homi K. Bhabha* (supra) and *Devendra Kothari* (supra), confirmed the order of the AO disallowing the claim of the assessee of Rs.26,04,585/- on account of PMS fees paid against capital gains.

5. Before us, the Ld. counsel of the assessee submits that the issue is covered in favour of the assessee by the judgment dated 04.05.2017 of the Hon'ble Gujarat High Court in *Principle CIT v. Sintex Industries Ltd*. (TA No. 291 of 2017). It is stated by him that in the aforesaid case, the Hon'ble High Court has held that when the assessee incurred expenses towards consultancy charges in order to make investment, the AO was not justified in treating and considering the expenses incurred towards consultancy charges as capital expenditure disallowable u/s 37 of the Act. Reliance is also placed by him on the order of the Pune Bench of the Tribunal in *KRA Holding & Trading Pvt. Ltd* (supra).

6. On the other hand, the Ld. DR submits that the case of the assessee in the instant appeal is distinguishable from *Sintex Industries Ltd*. (supra), in view of the fact that the issue therein was whether the AO was justified in treating and considering the expenses incurred towards consultancy charges as capital expenditure disallowable u/s 37 of the Act. It is submitted by him that herein the issue is whether the AO is right in disallowing the assessee's claim of Rs.26,04,585/- on account of PMS fees against capital gains.

The Ld. DR further submits that the decision in the case of *KRA Holding and Trading (P.) Ltd.* (*supra*) has been distinguished by the

Mumbai Bench of the Tribunal in the case of *Pradeep Kumar Harlalka* [IT Appeal No. 4501 (Mum.) of 2010].

7. We have heard the rival submissions and perused the relevant materials on record. The reasons for our decision is given below.

We begin with the decisions relied on by the Ld. counsel of the assessee. In the case of *Sintex Industries Ltd*. (supra), one of the issues raised was "whether the Tribunal erred in law and on facts in deleting the disallowance of expenditure of Rs.24,37,500/- incurred towards consultancy charges?". The AO made a disallowance of the above sum of Rs.24,37,500/- incurred towards consultancy charges u/s 37 by treating the same as capital expenditure. In appeal, the Ld. CIT(A) deleted the disallowance made by the AO by observing that the expenditure incurred by the assessee towards consultancy charges was purely revenue in nature and therefore, was an allowable expenditure. In further appeal, the Tribunal held as under:

> "We have duly considered rival contentions and gone through the record carefully. No doubt, the expenses were incurred by the assessee towards consultancy charges for making investment. On sale of investment, capital gain would arise to the assessee, but the expenses incurred by the assessee are not directly linked to the purchase of investment. These are paid for consultancy. If the expenses are not to be capitalized in the investment, then how the assessee will get this set off. Therefore, the learned CIT [A] has rightly observed that the expenses were not incurred towards purchase of investment, rather, these were incurred towards consultancy charges in order to keep track on the investment. Therefore, we do not see any error in the order of the learned CIT [A]. This ground of appeal is rejected."

In appeal by the revenue, the Hon'ble High Court agreed with the order of the Tribunal deleting the disallowance of Rs.24,37,500/- incurred by the assessee towards consultancy charges.

We find that the case of the assessee in the instant appeal is distinguishable from the above decision in view of the fact that the issue therein was whether the AO was justified in treating and considering the expenses incurred towards consultancy charges as capital expenditure disallowable u/s 37 of the Act, whereas the issue herein is whether the AO is right in disallowing the assessee's claim on account of PMS fees against capital gains.

7.1 The Ld. counsel has placed reliance on the decision of ITAT, Pune in *KRA Holding and Trading (P.) Ltd.* (*supra*) which has been distinguished by ITAT, Mumbai in the case of *Pradeep Kumar Harlalka* (supra) as under:—

> "13. Coming to the decision of Pune Bench of the Tribunal in the case of *KRA Holding & Trading (P.) Ltd.* (*supra*), after perusing the judgment very carefully we find that in that decision the decision of co-ordinate Bench of Mumbai Tribunal in the case of *Devendra Motilal Kothari* (*supra*) was distinguished mainly on the basis of decision of Hon'ble Bombay High Court in the case of *Smt. Shakuntala Kantilal* (*supra*). The Pune Bench referred to various paras of Hon'ble Bombay High Court's decision in para-22 and ultimately concluded in para-23 that what was required was that the claim should be bona fide and claim for such genuine expenditure has to be allowed so long as incurring of the expenditure is a matter of fact and necessity. However, as pointed out by the Ld. DR this decision was specifically overruled by the Hon'ble Bombay High Court in the case of *Roshanbabu Mohd. Hussein Merchant* (*supra*) and at placitum 18 it has been observed as under:

'As regards the decisions of this court in the case of *CIT* v*. Shakuntala Kantilal* [1991] 190 ITR 56 followed in the case of *Abrar Alvi* [2001] 247 ITR 312] and the decision of the Kerala High Court in the case of *Smt. Thressiamma Abraham (No. 1)* [2001] 227 ITR 802 which are strongly relied upon by the counsel for the assessee, we are of the opinion that the said decisions are no longer good law in the light of the subsequent decisions of the apex court referred to hereinabove.'

Thus, without going into further details we would only like to observe that the decision in the case of *Smt. Shakuntala Kantilal* (*supra*) is no more a good law in view of the latest decision and therefore that decision cannot be relied for the proposition that necessity of expenditure would make the same allowable."

7.2 Then we turn to the decisions relied on by the Ld. DR. In *Devendra Motilal Kothari* (supra), the assessee filed his return wherein certain amount was shown as short term capital gain and long term capital gain arising from sale of shares. During the course of assessment proceedings, the AO found that the fees paid for PMS was added by the assessee to the purchase cost of shares while computing the LTCG and STCG. The Assessing Officer disallowed the deduction claimed by the assessee on account of fees for PMS while computing LTCG and STCG holding that the same was not part of cost of acquisition of shares. On appeal, the Commissioner (Appeals) upheld the order passed by the Assessing Officer. On second appeal, the Tribunal held :

"The profit arising to the assessee on sale of shares and securities was chargeable to tax under the head 'capital gains' and this position was not in dispute. The only dispute was whether the fees paid by the assessee for PMS could be allowed as deduction in computing such income or not. The charge of income-tax is created by virtue of the provisions contained in section 4

according to which the income-tax is charged for the relevant assessment year in accordance with and subject to the provisions of Act in respect of the total income of the relevant previous year of every person. As per the scheme of the Act, income is broadly classified under five different heads and the income chargeable to tax under these heads has to be computed as per the relevant provisions applicable to respective heads of income. Section 45 to section 55A falling under Chapter IV-E deal with assessment of income under the head 'capital gains' and section 48 in particular prescribes the mode of computation of capital gains. As provided in section 48, expenditure incurred wholly and exclusively in connection with transfer and the cost of acquisition of the asset and cost of any improvement thereto are deductible from the full value of the consideration received or accruing to the assessee as a result of transfer of the capital assets. [Para 12]

In the instant case, the deduction on account of fees paid for PMS had been claimed by the assessee as deduction in computing capital gains arising from sale of shares and securities. He however had failed to explain as to how the said fees could be considered as cost of acquisition of the shares and securities or the cost of any improvement thereto. He had also failed to explain as to how the said fees could be treated as expenditure incurred wholly and exclusively in connection with sale of shares and securities. On the other hand, the basis on which the said fees was paid by the assessee showed that it had no direct nexus with the purchase and sale of shares and as rightly contended by the revenue, the said fees was payable by the assessee going by the basis thereof even without there being any purchase or sale of shares in a particular period. As a matter of fact, when the Commissioner (Appeals) required the assessee to allocate the fees paid for PMS in relation to purchase and sale of shares as well as in relation to the shares held as investment on the last date of the previous year, the assessee could not furnish such details nor could he give any definite basis on which such allocation was possible. Having regard to all these facts of the case, it

was opined that the fees paid by the assessee for PMS was not in extricably linked with the particular instance of purchase and sale of shares and securities so as to treat the same as expenditure incurred wholly and exclusively in connection with such sale or the cost of acquisition/improvement of the shares and securities so as to be eligible for deduction in computing capital gains under section 48. [Para 13]

At the time of hearing, the assessee raised an alternative contention in support of his claim for deduction on account of fees paid for PMS in computing the capital gains relying on the theory of real income and the rule of diversion of income by an overriding title. He contended that the fees for PMS being contractual liability directly relatable to the capital gains, there was a diversion of income from capital gain by an overriding title to the extent of the amount of such fees and the same, therefore, was not the income belonging to the assessee which was chargeable to tax under the head 'capital gains'. In this regard, it can be said that even though the assessee was under an obligation to pay the fees for PMS, the mere existence of such obligation to pay the said amount was not enough for the application of the rule of diversion of income by an overriding title. The true test for applicability of the said rule is whether such obligation is in the nature of a charge on source, i.e., the profit earning apparatus itself and only in such cases where the source of earning income is charged by an overriding title, the same can be considered as diversion of income by an overriding title. [Para 15]

In the instant case, the profit arising from the sale of shares was received by the assessee directly which constituted its income at the point when it reached or accrued to the assessee. The fee for PMS on the other hand was paid separately by the assessee to discharge his contractual liability. It was thus a case of an obligation to apply income which had accrued or arisen to the assessee and the same amounted to a mere application of income. Therefore, it was to be held that the payment of fees by the assessee for PMS did not amount to diversion of income by overriding title and the contentions

raised by the assessee in this regard could not be accepted being devoid of any merit. [Para 17]

As regards the contention of the assessee in support of claim for deduction on account of fees paid for PMS based on real income theory, the revenue rightly submitted that the theory of real income could not be applied to allow deduction to the assessee which was otherwise not permissible under the Act. In the case of CIT v. Udayan Chinubhai [1996] 222 ITR 456/88 Taxman 114 (SC), it was held by the Supreme Court in the similar context that what is not permissible in law as deduction under any of the heads cannot be allowed as a deduction on the principle of real income theory. [Para 18]

For the reasons given above, it was to be held that the fees paid by the assessee for PMS was not deductible in computing the capital gains as rightly held by the Assessing Officer. The impugned order of the Commissioner (Appeals) confirming the disallowance made by the Assessing Officer on this issue was to be therefore upheld dismissing the appeal filed by the assessee. [Para 19]

7.3 In *Homi K. Bhabha* (supra), the assessee declared gross long term capital gain of Rs. 67,32,921 and short term capital gain of Rs. 91,87,735. Thereafter a deduction was claimed in respect of professional fees / profit sharing fees paid to ENAM Asset Management Co. Ltd. for rendering portfolio management services. The AO observed that the PMS and Profit sharing fees (hereinafter collectively called as 'fees') paid to portfolio manager was unrelated to any profit or loss under the head 'Capital gains'. There is no dispute on the fact that the assessee claimed long term capital gain as exempt, which was duly accepted. The A.O. did not allow deduction for fees of Rs. 17,95,185 claimed by the assessee against the short term capital gain, as it was, in his opinion, not related

to the transactions resulting in to capital gain. It was argued before the learned CIT(A) that the assessee was entitled to deduction on account of fees against the short term capital gain, as it was directly related to sale of shares and hence should be taken as expenditure incurred wholly and exclusively in connection with transfer of shares. An alternative argument for considering it as diversion of income by overriding title, was also raised. The learned CIT(A) was unconvinced with the assessee's submissions. He echoed the assessment order on this point by holding that such charges could not be allowed as deduction u/s 48. On second appeal, the Tribunal observed that same issue had been predominantly decided in Devendra Motilal Kothari (supra) and Pradeep Kumar Harlalka (supra) against assessee after making thorough analysis of issue and, dealing with all aspects now raised by assessee and therefore, it thought as not proper to revisit all relevant facts and legal position in the above case with a view to test the correctness of above orders. On that reasons, the Tribunal sustained the disallowance made by the AO.

7.4 In *Capt. Avinash Chander Batra v. DCIT* (2016) 68 taxmann.com 366 (Mumbai-Trib), it has been held that PMS fee paid by assessee to various portfolio managers could not be allowed as deduction while computing capital gain arising from sale of shares kept in portfolio management services accounts held with various funds.

7.5 The Hon'ble Bombay High Court has held in *Panjumal Hassomal Advani v. Harpal Singh Abnashi Singh Sawhney*, AIR 1975 Bom 120 that a Co-ordinate Bench cannot refuse to follow an earlier decision on the

ground that it is incorrect and/or rendered on mis-representation. This for the reason that the decision of a Co-ordinate Bench would continue to be binding till it is corrected by a High Court. Also in *HDFC Bank Ltd. v. DCIT* (2016) 383 ITR 529 (Bom), the Hon'ble Bombay High Court has stated at page 545 that the above principle laid down in respect of a Co-ordinate Court would apply with greater force on subordinate Courts and Tribunals.

8. Facts being identical, we follow the order of the Co-ordinate Bench in *Devendra Kothari, Homi K. Bhabha, Pradeep Kumar Harlalka and Capt. Avinash Chander Batra* narrated hereinbefore and uphold the order of the Ld. CIT(A).

9. In the result, the appeal is dismissed.

Order pronounced in the open Court on 30/05/2018.

Sd/-	Sd/-
(SAKTIJIT DEY)	(N.K. PRADHAN)
JUDICIAL MEMBER	ACCOUNTANT MEMBER

Mumbai;
Dated: 30/05/2018
Rahul Sharma, Sr. P.S.

Copy of the Order forwarded to :

1. The Appellant
2. The Respondent.
3. The CIT(A)-
4. CIT
5. DR, ITAT, Mumbai
6. Guard file.

BY ORDER,

//True Copy//

(Dy./Asstt. Registrar)
ITAT, Mumbai