IN THE INCOME TAX APPELLATE TRIBUNAL
BENCH 'B' CHENNAI

ITA No.2167/Mds/2010
Assessment Year: 2005-2006

DEPUTY COMMISSIONER OF INCOME TAX
COMPANY CIRCLE-I(1), CHENNAI-600034

Vs

M/s AIG HOME FINANCE INDIA LTD
(FORMERLY M/S WEIZMANN HOMES LTD)
2nd FLOOR, CITI TOWERS, 117
SIR THYAGARAYA ROAD
T NAGAR, CHENNAI-600017
PAN NO:AAACW1328G

O K Narayanan, VP and George Mathan, JM

Dated: May 5, 2011

ORDER

Per: George Mathan:

I.T.A. No. 2167/Mds/2010 is an appeal filed by the Revenue against the order of ld. Commissioner of Income Tax (Appeals)-III, Chennai in appeal No.4/2010-11/A.III dated 30.9.2010 for the assessment year 2005-06.

2. Shri K.E.B. Rengarajan, Junior Standing Counsel represented on behalf of the Revenue and Shri G.S.D. Babu, C.A. represented on behalf of the assessee.

3. In this appeal, the Revenue has raised the following grounds:-

1. The Order of the learned Commissioner of Income Tax (Appeals) is contrary to the Law and facts of the case.

2. The learned CIT(A) has erred in deleting the disallowance of Rs. 1,00,03,428/- made u/s.40A(2)(b) being syndication charges/ guarantee fee paid to M/s Weizmann Ltd.

2.1 The learned CIT(A) ought to have appreciated the fact that 'Weizmann Ltd., is the promoter of the assessee company and is a major stake holder and it is not clear as to why the assessee company approached through the associate concerns for raising loans when it should have directly approached the Banks for any loans or financial needs. Moreover, the assessee company itself is an established company and has been engaged in the banking business for over last 10 years. Therefore, the sum paid to the sister concern merely for providing corporate guarantee etc., is not justified.

2.2 It is submitted that Section 40A(2)(b) clearly disallows excessive expenditure or unreasonable having regard to the fair market value of the goods, services or facilities.

2.3 It is further submitted that while some of the major stake holders of the assessee company viz., Federal Bank and Asian Finance & Invt. Corp. a unit of Asian Dev. Banks are finance companies, the other major stake holder M/s Weizmann Ltd., is engaged only in the manufacturing and export of textiles and is nothing to do with the business of banking.

2.4 The learned CIT(A) ought to have seen that as per the Circular No.6P(LXXVI-66) of 1968 which the assessee has quoted for its benefit clearly states that Sec.40A(2)(b) were introduced to keep a check on excessive and unreasonable payments to related concerns.

3. The learned CIT(A) has erred in restricting the disallowance on staff welfare expenses to Rs. 1,50,000/- as against the disallowance of Rs. 6,47,029 made by the assessing officer.

3.1 Having regard to Rule 46A, an opportunity ought to have been given to the assessing officer to submit report on the evidences not produced during the course of assessment proceedings.

4. The learned CIT(A) has erred in deleting disallowance of Rs. 1,81,934/- being 50 of the brokerage expenses paid.

4.1 It is submitted that the learned CIT(A) has relied on the assessee's argument that the brokerage of 2% of the deposits mobilised, is permissible as per the directive issued by the National Housing Bank and as per the National Housing Bank Act, 1987. The above said Act states that 2% of the brokerage is only permissible. As per assessing officer's contention it was not possible to ascertain from the details furnished by the assessee whether the recipients actually mobilised any deposits for the deposits for the appellant or not.

4.2 In this issue, also having regard to Rule 46A, an opportunity ought to have been given to the assessing officer to submit report on the evidences not produced during the course of assessment proceedings.

4.3 It is further submitted that the brokerage is only for the deposits mobilised. In this case, since the nexus between the deposits mobilised for the brokerage paid cannot be ascertained, the assessing officer's contention would be correct.

5. The learned CIT(A) has erred in deleting the disallowance of Rs. 1,21,60,250/- being claim of deduction of u/s. 36(1)(viii).

5.1 The learned CIT(A) ought to have appreciated that as per the provisions of Section 36(1)(viii) "any special reserve created and maintained by a specified entity, an amount not exceeding 20% of the profits derived from eligible business computed under the head 'profits and gains of business or profession {before making any deduction under this clause} carried to such reserve account".

5.2 It is submitted that "Specified entity" means, a Banking Company or a Finance Company or any other finance corporation specified in Sec.4A of the Companies Act and whose business is providing long-tem finance for construction and purchase of houses in India for residential purposes as per Sec. 36(1)(viii)(bii) of the Income-tax Act and business of providing long-term finance for development of infrastructure facility in India as per 36(1)(viii)(bii) of the Act.

5.3 It is further submitted that "Eligible Business" means "in respect of specified entity the business of providing long term finance for industrial or agricultural development or development of infrastructure facility or construction or purchase of house in India for residential purpose". Accordingly, the deduction under this chapter is available only in respect of income derived from long-term finance of construction or house to be used for residential purposes meaning thereby any income other than the Income from housing loan etc. is not eligible for deduction under these section. Apart from housing loan, the Company also extends loan for two wheelers, consumable durables and also earns interest on deposits made with other Banks which incomes are not eligible for deduction u/s. 36(1)(viii).

5.4 The learned CIT(A) ought to have seen that as far as the securitization of income is concerned it is nothing but the discounted value of interest income on the assets securitize for 10 years period, received upfront. The assessing officer's contention of the securitization income cannot be held as derived from longterm housing finance for the simple reason that this activity is in the nature of pledging the security in respect of housing loan already granted to the other banks and releasing further loan which might have been used for purposes by the assessee, and denied deduction u/s. 36(1)(viii), which, ought to have been considered by the Ld. CIT(A).

6. For these and other grounds that may be adduced at the time of hearing, it is prayed that the Order of the learned Commissioner of Income Tax (Appeals) be set aside and that of the Assessing Officer be restored.

4. In regard to ground Nos. 2 to 2.4, it was submitted by the ld. Junior Standing Counsel that the assessee had made payments of syndication charges/guarantee fee to M/s Weizmann Ltd. It was a submission that the A.O. had invoked the provisions of Section 40A(2)(b) of Income-tax Act, 1961 (hereinafter called "the Act") and held that 0.5% of the guarantee fee paid to M/s Weizmann Ltd. was not allowable. It was a submission that the syndication charges/guarantee fee paid to M/s Weizmann Ltd. was to the tune of Rs. 1,00,03,428/-. It was a submission that M/s Weizmann Ltd. was promoter of assessee-company and it should have provided services at free of cost to the assessee. It was also submission that the A.O. had observed that leading banks and financial institutions were also share holders of assessee-company, it could have raised loans directly from banks. It was submission that the assessee had also paid an amount of Rs. 29,82,737/- to third parties for rendering similar services as rendered by M/s Weizmann Ltd. and the said commission was at the rate of 0.5% to 1%. It was the submission that according to National Housing Board, the companies which were doing business of housing finance were liable to pay guarantee commission of 0.5% for the loans guaranteed by the National Housing Board. It was submission that the A.O. had disallowed the whole of the guarantee fee paid by the assessee to M/s Weizmann Ltd. He vehemently supported the order of the A.O.

5. In reply, the learned A.R. submitted that even though the provisions of Section 40A(2)(b) of the Act had been invoked, the whole of the guarantee fee had been disallowed and no comparison had been made by the A.O. It was the submission that as per provisions of Section 40A(2)(b) of the Act, a reasonable amount was liable to be allowed. It was further submission that other banks were paying guarantee fee of 1.5% for guaranteeing loans taken by small and medium enterprises. It was further submission that no disallowance was called for in the case of the assessee. He vehemently supported the order of the ld. CIT(Appeals).

6. We have considered the rival submissions. A perusal of provisions of Section 40A(2)(b) of the Act shows that this provision is applicable where an A.O. is of the opinion that the payment is excessive or unreasonable when such payments had been made to related parties. Here, the A.O. has not shown how the payment made by the assessee to M/s Weizmann Ltd. was unreasonable or excessive. In fact, a perusal of the order of the ld. CIT(Appeals) clearly shows that he has taken into consideration that the National Housing Board, which is the accredition authority for finance companies doing the business of long term housing finance, has permitted 0.75% of guarantee fee for providing loans availed by housing finance companies. Public sector banks are also charging 1.5% for providing guarantee cover. It is also noticed that the ld. CIT(Appeals) has taken into consideration the fact that the A.O. has not doubted the fees paid to third parties for providing identical range of services especially when such fee was between 0.5% to 1%. In the circumstances, we are of the view that 0.5% of guarantee fee paid to M/s Weizmann Ltd. by the assessee is not excessive or unreasonable but is well within the range as paid by the assessee to third parties and much lower than the percentage fixed by National Housing Board, which itself is an undertaking promoted by Reserve Bank of India. Therefore, we are of the view that the findings of the ld. CIT(Appeals) on this issue in deleting the disallowance is on right footing. Hence, the same is upheld. Thus ground Nos.2 to 2.4 are dismissed.

7. In regard to ground Nos.3 and 3.1, it was submitted by the ld. Junior Standing Counsel that the A.O. had, in the course of assessment proceedings, disallowed Rs. 1,50,000/- out of the staff welfare expenses claimed by the assessee. It was a submission that the ld. CIT(Appeals) had deleted the disallowance out of the same, to an extent of Rs. 1,00,000/-. It was a further submission that the A.O. had also made a further disallowance of Rs. 2,00,000/- out of the expenditure incurred by the assessee on account of reimbursement of leave travel allowance, medical, etc. paid to staff and the ld. CIT(Appeals) had deleted Rs. 1,00,000/- out of the said disallowance. It was submitted that the ld. CIT(Appeals) ought not to have deleted the disallowance made by the A.O.

8. In reply, the learned A.R. submitted that the disallowance was on an ad hoc basis and in regard to bills and vouchers, it was submitted that the A.O. had not called for any bills and vouchers in this case. It was further submitted that even though the Revenue has raised an issue of Rule 46A in regard to entertaining of additional evidence by the ld. CIT(Appeals), no additional evidence had been produced. He vehemently supported the order of the ld. CIT(Appeals).

9. We have considered the rival submissions. A perusal of the order of the ld. CIT(Appeals) in para 5.2 and 5.3 clearly shows that no fresh evidence had been considered by the ld. CIT(Appeals). In fact, the ld. CIT(Appeals) had deleted a part of the addition as the same had been made on ad hoc basis. It is further noticed that

the turnover of the assessee for the assessment year under consideration itself was more than Rs. 34 Crores. The staff welfare expenses incurred by the assessee was only about Rs. 19.26 lakhs and on leave travel allowance and medical expenses, the expenditure was Rs. 4.5 lakhs. The Revenue has also not rebutted the findings of the ld. CIT(Appeals) that the A.O. had not called for any vouchers and the disallowance has been made only on ad hoc basis. In the circumstances, we are of the view that the action of the ld. CIT(Appeals) in confirming Rs. 50,000/- out of the staff welfare expenses and Rs. 1,00,000/- out of the other expenses, is on right footing and does not call for any interference. Thus ground Nos.3 and 3.1 stand dismissed.

10. In regard to grounds No.4 to 4.3, it was submitted by the ld. Junior Standing Counsel that the assessee had made a payment of brokerage at 2% of the deposits mobilised. It was submitted that the brokerage expenditure was to an extent of Rs. 3,63,868/- and the same had been paid to different persons. He further submitted that the A.O. had disallowed 50% of the said expenditure and ld. CIT(Appeals) had deleted the said disallowance. He vehemently supported the order of the A.O.

11. In reply, the learned A.R. submitted that as per the guidelines provided by the National Housing Board, the assessee was entitled for pay 2% brokerage and in fact, the A.O. had also, in principle, allowed the payment of the commission and he disallowed only 50% of the said brokerage. The learned A.R. vehemently supported the order of the ld. CIT(Appeals).

12. We have considered the rival submissions. A perusal of the assessment order clearly shows that the disallowance made out of the brokerage expenses was on the ground that the payment of brokerage on mobilisation of public deposits by a banking company has never been heard of as also on the ground that it was not ascertainable whether the recipients actually mobilised any deposits for the assessee-company or not. The fact that the National Housing Board has permitted 2% brokerage on the deposit mobilisation clearly shows that paying brokerage on the mobilisation of public deposits by a banking company is an accepted norm. Further, if the A.O. did not believe the payment of brokerage to eight persons, he should have disallowed the full amount. There is also no finding by the A.O. that the payments were not genuine or that the payments were bogus. Once the payment has been accepted as brokerage for mobilisation of deposits, the same cannot be disallowed in part. In the circumstances, we are of the view that the findings of the ld. CIT(Appeals) on this issue is on right footing and does not call for interference. Thus ground Nos.4 and 4.3 stand dismissed.

13. In regard to ground Nos.5 to 5.4, it was submitted by the ld. Junior Standing Counsel that in the course of assessment, the A.O. had restricted the claim of deduction under Section 36(1)(viii) of the Act. It was a submission that the A.O. had treated the securitization income of the assessee as not being eligible for claim of deduction under Section 36(1)(viii) of the Act. It was submitted that the deduction under Section 36(1)(viii) of the Act was not allowable to the assessee as the same was not derived from the long term housing finance but was practically received from the business of pledging the security in respect of housing loan already granted to other banks and releasing further loans which might have been used for any purpose.

14. In reply, the learned A.R. submitted that for the purpose of deduction under Section 36(1)(viii) of the Act, the main criteria were that – (i) deduction is available

only for financial corporations/public companies engaged in providing long term finance for certain purpose; (ii) a special reserve is to be created and maintained; (iii) the deduction is restricted to 40% of the profits derived from the business of long term finance computed under the head 'profits and gains of business or profession" and carried to such special reserve. It was a submission of the learned A.R. that when the assesseecompany complied with all the conditions, the securitization income was rightly held by the ld. CIT(Appeals) to be included in computing the income from housing finance. He vehemently supported the order of the ld. CIT(Appeals).

15. We have considered the rival submissions. As per Explanation (a) to Section 36(1)(viii) of the Act, the assessee is a housing finance company. The assessee has also been accredited under accredition authority being the National Housing Board. As per the provisions of Explanation (b) and (c) to Section 36(1)(viii) of the Act, 'eligible business' means the business of providing long term finance for the construction or purchase of houses in India for residential purposes. It is an undisputed that the securitization is of the long term housing loan. In the process of securitization, the future receivables for a period of ten years are discounted with banks and the banks pay the Net Present Value of future receivables to the assessee as part of securitization arrangement. What is to be understood is that the long term housing loan granted by the assessee to the borrowers is discounted with third party banks. The risk continues to remain with the assessee as in the event of default by the borrowers, the assessee is responsible to make good to default to banks. The Net Present Value at which the long term housing loans are discounted had nothing but the future interest income discounted to the present value. Thus, the securitization amount is nothing but the interest on the housing loan which is discounted to the present net value. This amount would obviously be the income of the assessee from the long term housing loan disbursed by the assessee. In the circumstances, we are of the view that the securitization income is an income from business of long term housing finance. We are of the view that the same is eligible for deduction under Section 36(1)(viii) of the Act. Therefore, we uphold the finding of the ld. CIT(Appeals) in deleting the disallowance of the claim of deduction under Section 36(1)(viii) of the Act, which is on right footing and does not call for any interference. Thus ground Nos.5 to 5.4 stand dismissed.

16. Ground Nos.1 and 6 are general in nature and require no adjudication.

17. In the result, the appeal filed by the Revenue stands dismissed.

(The order was pronounced in the Court on 5.5.2011)