

AO couldn't disallow part of expense if it was incurred wholly & exclusively for business purpose

Summary – The Hyderabad ITAT in a recent case of Fincity Investments (P.) Ltd., (the Assessee) held that where expenditure claimed by assessee towards service charges was proved to be wholly and exclusively for purpose of business, same was to be allowed

Facts

- The assessee investment company filed its return of income and claimed expenses under the head 'administrative and other expenses,' of sum of Rs. 18 lakhs towards service charges paid to SRSR for the services like advisory services in its business area, accounting services, collection of interest and dividend, taxation, ROC related matters and maintenance of its land properties etc.
- The Assessing Officer was of the opinion that the directors of SRSR were related persons to the directions of assessee-company. The Assessing Officer held that the service charges paid were disproportionate to the services received and therefore, entire expenditure of Rs. 18 lakhs could not be said to be expended wholly and exclusively for the purpose of business in terms of section 37(1). The Assessing Officer estimated sum of Rs. 3 lakhs as reasonable expenditure considering the nature and volume of business of assessee and the nature of services rendered by SRSR. The balance was disallowed under section 37(1)
- On appeal, the Commissioner (Appeals) also confirmed the disallowance made by the Assessing Officer.
- On second appeal:

Held

- As far as the issue of claim of professional charges to SRSR is concerned, the Assessing Officer accepts that there were certain services rendered by SRSR to assessee-company. He had allowed an amount of Rs. 3 lakhs as against the claim of assessee. Thus, there is no dispute between the parties that SRSR has rendered some services for which payment was born by assessee. The issue is about the quantum of allowance as there is no dispute about services being rendered. According to section 37(1), any expenditure (not being expenditure of the nature described in sections 30 to 36 and not being in the nature of capital expenditure or personal expenses of the assessee), laid out or expended wholly and exclusively for the purposes of the business or profession shall be allowed in computing the income chargeable under the head 'Profits and gains of business or profession'. The expression 'wholly' in section 37(1) has been used with reference to the quantum, while the expression 'exclusively' refers to the nature or the purpose of the activity in which the expenditure is incurred. In other words, the whole of the expenditure must have been solely and exclusively incurred for business purposes, in order to qualify for allowance under section 37(1). The expression 'wholly & exclusively' used in section 37(1) does not mean 'necessary'. Ordinarily, it is for the

assessee to decide whether any expenditure should be incurred in the course of his or its business. Such expenditure may be incurred voluntarily and without any necessity and if it is incurred for promoting the business and to earn profits assessee can claim deduction even though there was no compelling necessity to incur such expenditure. Though the main objects of business is to earn profits, business purposes are wider than profit-making purposes. Business expediency does not require that expenses should be incurred only for earning immediate profits. Expenses incurred though not directly related to earning to income, may be allowable deductions if they are related to the carrying on of the business. It is for the assessee to decide how best to protect its own interest. It is not open to Assessing Officer to prescribe what expenditure an assessee should incur and in what circumstances he should incur that expenditure. Expression 'commercial expediency' is not a term of art. It means everything that serves to promote commerce and includes every means suitable to that end. In applying the test of commercial expediency for determining whether the expenditure was wholly and exclusively laid out for the purposes of the business, reasonableness of the expenditure has to be adjudged from the point of view of the businessman and not of the revenue in deciding whether a payment of money is a deductible expenditure, one has to take into consideration questions of commercial expediency and the principles of ordinary commercial trading.

- The Assessing Officer cannot step into the shoes of assessee to re-fix the amount that should have been paid. There is no dispute that the amount was paid for the purpose of business, as Assessing Officer has allowed the amount partly. Since the provisions of section 37(1) does not have any restriction to allow the amount partly, so long as the expenditure was incurred for the purpose of the business wholly and exclusively, the same has to be allowed. The restrictions placed in other provisions like that section 36(1)(iii) for the purpose of interest, under section 40A (expenses or payment not deductible in certain circumstances) and also restrictions placed under sections 30 and 31 does not apply to the facts of the case. In view of that, the Assessing Officer has wrongly considered the claim. There was no power to Assessing Officer to reduce the claim, whereas he can examine whether the amount can be allowed or not in full. In view of that, since the restrictions under section 37(1) are not applicable, the whole of the amount claimed is to be allowed as the expenditure is not proved to be personal or capital in nature, as provided in the section itself. The Assessing Officer is directed to allow the claim in full. To that extent, the orders of Assessing Officer and Commissioner (Appeals) were modified. Thus, the grounds on this issue were allowed.