

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

BEFORE SHRI. VIJAY PAL RAO, JUDICIAL MEMBER

AND

SHRI. S. JAYARAMAN, ACCOUNTANT MEMBER

I.T.A No.493/Bang/2014
(Assessment Year : 2010-11)

Deepak Cable (India) Ltd,
No.7, N8, Iyengar Street, Seshadripuram,
Bengaluru 560 020 .. Appellant
PAN : AAACD6466C

v.
Additional Commissioner of Income Tax,
Range-11, Bengaluru .. Respondent

I.T.A No.669/Bang/2014
(Assessment Year : 2010-11)

Additional Commissioner of Income Tax,
Range-11, Bengaluru .. Appellant

v
Deepak Cable (India) Ltd,
No.7, N8, Iyengar Street, Seshadripuram,
Bengaluru 560 020 .. Respondent
PAN : AAACD6466C

Assesseeby :Shri. Suresh Muthukrishnan, CA
Revenue by : Shri. Sanjay Kumar, CIT-III

Heard on : 08.02.2017
Pronounced on : 05.05.2017

ORDER

PER S. JAYARAMAN, ACCOUNTANT MEMBER :

These cross appeals are filed by the assessee and the Revenue, respectively, against the order of the CIT (A)-I, Bengaluru, for the assessment year 2010-11.

02. The assessee is engaged in the manufacture and sale of power transmission conductors and in erection and commissioning contracts which involves setting up of transmission lines and installation of Sub stations under tender from power distribution companies. For the assessment year 2010-11, it filed its return on 14.10.2010, declaring the total income at Rs.78,34,05,920/-. In the assessment made u/s 143(3) dt 31.01.2013, inter alia, the AO made disallowances ; u/s14A rw r 8D(2) (ii) at Rs.26,93,672/-, Rs.3,50,154/- u/s14A rwr 8D(2) (iii) & on professional expenses at Rs.2,59,47,337/-, capitalised the interest claim at Rs.7,15,44,313/- to capital work in progress and disallowed interest at Rs.2,27,14,151/- towards the amounts advanced to sister concerns. The AO also charged interest u/ss 243 A, B & C. The assessee filed an appeal before the CIT (A). The CIT (A) , out of the above issues, confirmed the disallowances made u/s14A rw r 8D(2) (iii) at Rs.3,50,154/- , on professional expenses at Rs.2,59,47,337/- and levy of interest u/ss 243A, B & C and deleted all other disallowances. Aggrieved, the assessee filed appeal with the following grounds:

1. That the order of the Authorities below in so far as it is against the appellant is against the law, facts, circumstances, natural justice, equity, without jurisdiction and all other known principles of law.
2. The total income computed and the total tax computed is hereby disputed.
3. The Learned CIT(A) and AO erred in making disallowance u/s 14Ar.w.r 8D(2)(iii) of the Act amounting to Rs. 3,50,154/-.
4. The Learned CIT(A) and AO erred in disallowing professional expenses to the extent of Rs. 2,59,47,337/- overlooking the services rendered and the accrual system of accounting followed by the appellant.
5. The appellant denies the liabilities for interest u/s 234A, 234B, & 234C. Further prays that the interest should be levied only on returned income.

03. Aggrieved by the CIT(A) order, the Revenue also filed an appeal with the following grounds :

2. The CIT(A) erred in deleting the disallowance of Rs 23,43,518 calculated under rule 8D(2)(ii) holding that none of the interest payments claimed by the assessee can be taken for the purpose of rule 8D(2)(ii) without appreciating the fact that the finance charges included Rs 15,83,33,480 and Rs 7,98,,57,413 towards interest on cash credit and interest to others respectively and also without appreciating the provisions of Section 14A read with Rule 8D(2)(ii) in its true sense and right spirit and the fact that when interest expense incurred cannot be directly attributed to any particular income or receipt, rule 8D(2)(ii) will be applicable.
3. The CIT(A) erred in not appreciating the fact that investments are made from a common pool of funds ,i.e., working capital and / or cash credit or overdraft accounts and the provisions of Rule 8D(2)(ii) are automatically applicable as held in the case of **Champion Commercial Ltd 139 ITD 108 (Kol)** which clarified that *common interest expenses which are to be allocated in terms of the formula under rule 8D(2)(ii) will be only such interest expenses as are neither directly attributable to borrowings specifically used for tax exempt incomes or receipts nor are directly attributable to borrowing specifically used for taxable incomes or receipts.*
4. The CIT(A) erred in deleting the addition of Rs.7,15,44,133/- by holding that no interest could be disallowed as interest free funds were utilized for work-in-progress without appreciating the fact that the assessee failed to bring out conclusive evidence to prove that only interest free funds were utilized for capital WIP.
5. The CIT(A) erred in holding that the AO was not justified in disallowing interest of Rs 2,27,14,151 on advances given to sister concerns on the ground that the loan advanced to its sister concerns were out of interest free funds only, without appreciating the fact that when sufficient interest free funds were available with the assessee it was not commercially expedient to borrow interest bearing funds on the one hand and extend interest free advances to its sister concerns on the other.
6. The CIT(A) erred in holding that the AO was not justified in disallowing interest of Rs 2,27,14,151 on advances given to sister concerns on the ground that the loan advanced to its sister concerns were out of interest free funds only which is based on the assumptions of the CIT(A) and without any conclusive evidence as the assessee failed to bring out any cogent evidence

7. The CIT (A) erred in not appreciating that his decision that the major loan given to Brindavan Hydro Power Ltd is for business exigencies for the only reason that the assessee is engaged in generation and sale of wind power is without any valid evidence.

04. The AR submitted that AO noted that the assessee had made investments in shares of M/s. Brindavan Hyderabad Power Ltd. yielding tax-free income and that the investments were made out of borrowed capital. The AO rejected the assessee's contention that it had made the investment out of its own funds and internal accruals on the ground that the cash flow statement filed by it showed negative cash flow and that, even if the assessee's statements were true, mandatory disallowance was called for u/s.14A r w r 8D. Thus, the AO invoked section 14A and applied the formula prescribed in rule 8D of the Rules and disallowed Rs.26,93,672/- u/s14A r w r 8D(2) (ii) and Rs.3,50,154/- u/s14A r w r 8D(2) (iii). On the assessee's appeal, the CIT(A) on going through its balance sheet as on 31.03.2009 and 31.03.2010, found its financial position as under :

	31.03.2010	31.03.2009
Share capital	9,16,92,300	9,16,92,300

Reserves and Surplus	4,69,71,42,807	4,29,24,80,527
Total	478,88,35,107	438,41,72,827
<u>Loan Funds</u>		
Secured loans	158,68,60,634	215,66,23,303
Unsecured loans	33,97,07,691	97,94,20,812
Total	192,65,68,325	313,60,44,115

From which, the CIT(A) found that the interest -free funds available as on 31.03.2010 has increased by Rs.40,46,62,280, vis a

the fund position as on 31.3.2009 while the investment made as on 31.03.2010 was at Rs.14,00,30,908 as against Rs.30,900 as on 31.03.2009. Since the assessee is having interest free funds for Rs.478 88,35,107, as such sufficient funds for making investment in shares and mutual funds are available. So, the CIT(A) found force in the assessee's submission that no borrowed funds have been utilised for making the investment of Rs.14,00,30,900/- on tax-free securities, the receipt from which is exempt from tax. The CIT(A) also noted that the assessee incurred the following indirect interest payment as per Schedule 18 of the Profit and Loss Account for the period ending 31/03/2008 :

PARTICULARS		
Interest on loans for a fixed period	Rs.	15,83,30,480
Interest on others	Rs.	7,98,57,413
Total	Rs.	23,81,90,983

and observed that the major amount of interest payment is towards working capital loan. Similarly, the assessee also paid interest on term loans. A perusal of the details of the said financial charges clearly indicates that the above interest payments are directly attributable to the earning of business income. Therefore, relying on the decision of the Hon'ble Tribunal of Kolkata Bench in the case of Champion Commercial Ltd. [139 ITD 108(Kol)], he held that none of the interest payments can be considered under Rule 8D(2)(ii) . Thus, the said payment cannot be attributed to the borrowing specifically used for tax

exempt income. There is no material / evidence on record to show the nexus between the borrowals and tax-free investments. Further, tax free investments are made during the year under consideration out of interest free funds as mentioned above. Therefore, the CIT(A) held that none of the interest payments claimed by the assessee can be taken for the purpose of Rule 8D(2)(ii) and hence deleted the disallowance of Rs.23,43,518/-. However, for the disallowances made u/s 14A rwr 8D(2) (iii) at Rs.3,50,154/-, the CIT(A) held that disallowance u/s 14A rwr 8D(2) (iii) is towards other expenses in the nature of indirect expenditure. The word 'expenditure' used in section 14A has a wider meaning and would take in its sweep not only expenditure but also all forms of expenditure regardless of whether it is fixed, direct, indirect, administrative, managerial or financial. Therefore, the said rule provides for the indirect expenditure as a fixed percentage of the average investments as per the formula laid down. As already stated, the AO has power to invoke rule 8D even in a case where the appellant claims that no expenditure has been incurred by him in relation to income which does not form part of the total income as per subsection (3) of section 14A of the Act. In the instant case, it is the contention of the assessee that no expenditure has been incurred for earning the exempt income. The same cannot be accepted because there may be some indirect expenditure, which is not directly visible. Since it is already decided that the term 'expenditure' in section 14A includes indirect expenditure, the AO's action in making a disallowance of

Rs.3,50,154/- is justified and is confirmed. The AR submitted that this is unwarranted.

05. On the associated issues and on the Revenue's appeal , the DR submitted that when the assessee's loan is not specific Rule 8D is applicable and in this regard, relied on 139 ITD 108Kol . The AO noted that the assessee had given advances at Rs.15,14,27,679/- to four sister concerns viz. M/s. Surya Transmission Ltd., M/s. Anchor Investment Aid Pvt. Ltd, M/s. Shah Brothers Merchant P. Ltd and M/s. Brindavan Hydropower P. Ltd. When asked for clarification, the assessee explained that the loan given to M/s. Brindavan Hydropower P. Ltd. was out of business expediency as it was its a subsidiary. On examination of the cash outflow statement, the AO found that the net increase in cash and cash equivalents was at Rs.53,79,13,980/- and Rs.114,95,06,440/-for the years ended 31/3/2009 and 31/3/2010 respectively; that the investments made in fixed assets subsidiary companies and loans given to subsidiary/sister concerns were made out of secured loans amounting to Rs.215.66 crores and Rs.158.68 crores as on 31/3/2009 and 31/3/2010 respectively; that the said investments and advances were made out of unsecured loans outstanding on 31/3/2009 and 31/3/2010 at Rs.97.94crores and Rs.33.97 crores respectively; that the aggregate loan liability of the appellant was more than Rs.212 crores and Rs.200 crores as on 31/3/2009 and 31/3/2010; and that all the loans viz, cash credit loans, overdraft loans and other unsecured loans are

indirect loans. The total indirect interest on cash credits and on other loans at Rs.15,83,30,480/- and Rs.7,98,57,413/- aggregated at Rs.23,81,90,893/-. The AO noted from the details furnished by the appellant that the average of capital work-in-progress between 31/3/2889 and 31/3/2010 amounted to Rs.47,69,68,892/-. Interest at 15% on this amount at Rs.7,15,44,133/- was held by the AO to be capital in nature and, by capitalising the same, he disallowed it.

5.1 However, the CIT (A) held that the average of capital work-in-progress between 31.03.2009 and 31.03.2010 worked out to Rs. 47,69,60,892. However, as per balance sheet work-in-progress as on 31.03.2009 at Rs. 18,36,76,200 and as on 31.03.2010 at Rs. 28,44,83,521 and average would be Rs.23,40,79,860. Thus, further increase in work-in-progress by Rs. 10,08,07,321, as per AO. Interest free fund as on 31.03.2010 at Rs. 478,88,35,107 and increase during the year shown at Rs. 40,46,62,280. On the other hand interest bearing funds reduced from Rs. 313,60,44,115 to Rs. 192,65,68,325. This fact indicates that interest free funds has been utilised for work-in-progress, hence no interest could be disallowable. Therefore, he deleted the addition of Rs. 7,15,44,133 .

5.2 On disallowance of interest free advances given to sister concerns at Rs.2,27,14,151, the DR submitted that the AO found that

the assessee had given advances to sister concerns at Rs.15,14,27,679/- free of interest out of funds borrowed by the assessee on interest. Applying the rate of interest at 15% on the advances so given, the AO disallowed a sum of Rs.2,27,14,151/- out of deduction claimed towards interest paid by it. The CIT (A) on perusal of the notes on account noted the amount of advance as under:-

Name of the party	3 1.03.2009	3 1.03.2010
Surya Transmission Ltd.	3,58,88,324	1,22,07,821
Anchor Investment Aid Pvt. Ltd.	2,42,817	2,42,817
Shah Brothers Merchant Pvt. Ltd.	87,360	1, 16, 115
Brindawan Hydro power pvt. Ltd.	-	20,33,26,399
Total	3,62,18,501	21,58,93,152

The CIT(A) held that it shows that loan and advance given to associated concern increased from Rs. 3,62,18,501 to Rs. 21,58,93,152 i.e. a sum of Rs. 17,96,74,651 further loans/advance made during the year. Since the appellant is having sufficient interest free funds the loan given to its sister concern was out of interest free fund only. Moreover, major loan given to M/s. Brindavan Hydro Power Limited is for business exigencies since the appellant company engaged in the wind power generation and sale.

5.3 On the above facts , the CIT(A) held that the AO was not justified in disallowing interest of Rs. 2,27,14,151/-and therefore he deleted that addition . The DR submitted that the CIT(A) considered all these issues on a simplistic manner and there is no

commercial expediency in advancing loan to Hydro power company , which is not the assessee's line of business. In this regard, he relied on the following decisions :

- i) Delhi ITAT decision in J. H. Fin-vest P. Ltd v. DCIT [(2014) 43 taxmann.com 210 (Delhi)], wherein the Tribunal held that where assessee claimed that no expenditure was incurred towards exempt income but it was found that major part of available funds was invested in shares of various companies, proportionate disallowance was called for.
- ii) The decision of Gujarat High Court in the case of CIT v. Arihant Avenue & Credit Ltd 9(2013) 36 taxmann.com 14], wherein the High Court held that where assessee had given interest-free advances to its sister concern but it was not case of revenue that interest bearing borrowed money was given as interest-free advance to those parties, no addition on account of notional interest income was warranted.
- iii) Jurisdictional High Court decision in the case of M/s. United Breweries Ltd v. DCIT in ITA No.419/2009, dt.31.05.2016, has upheld that section 14A is applicable even where the motive in acquiring the shares was to obtain controlling interest in the companies. It also upheld the findings that it is for the Assessing Officer to ascertain from the facts as to how *much interest bearing borrowings was utilized to acquire shares in the companies. It is also necessary to see as to whether any interest bearing borrowed funds were used in making the advances. The Assessing Officer may make the disallowance of interest u/s. 14A only if it is found that interest bearing borrowed funds were used to acquire shares in the companies or for making advances and the Board's Circular No 5/2014 dt 11.02.2014 issuing clarification regarding disallowance u/s14A.*

06. Per contra, the AR invited our attention to the cash-flow statement, which is extracted as under :

	For the year ended 31 March 2010	(Amount in Rs) For the year ended 31 March 2009
A) Cash flow (used in)/ generated from operating activities:		
Net profit before tax and prior period items	692,358,457	461,741,653
Prior period adjustments (other than income-tax charge and deferred tax credit) adjusted to accumulated balance of profit and loss account	-	(321,813,100)
Adjustments for:		
Depreciation	23,201,819	47,178,693
Unrealised foreign exchange loss	3,460,038	-
Interest income		
- on bank deposits and inter-corporate deposits	(25,290,651)	(29,131,100)
- on income-tax refund	-	(2,570,514)
(Profit)/ loss on sale of fixed assets, net	150,784	(154,833)
Interest on loans	238,190,893	266,915,471
Operating profit before working capital changes	932,071,340	422,166,270
Adjustments for:		
Increase in trade and other receivables	(83,147,987)	(2,649,459,480)
Decrease in inventories	6,316,430	37,709,818
Decrease in current liabilities and provisions	720,504,038	856,465,276
Cash (used in)/ generated from operations	1,575,743,821	(1,333,118,116)
Interest received on income-tax refund	-	2,570,514
Direct taxes paid, net of refund (including fringe benefit tax)	(359,649,630)	(854,236,943)
Net cash (used in)/ generated from operating activities (A)	1,216,094,191	(2,184,784,545)
B) Cash flow used in investing activities:		
Interest received	27,432,673	41,052,463
Purchase of fixed assets	(181,548,446)	(98,694,861)
Investment in subsidiary	(140,000,000)	-
Sale of fixed assets	112,889	199,920
Net cash used in investing activities (B)	(294,002,884)	(57,442,478)
C) Cash flow generated from/ (used in) financing activities:		
Secured loans repaid to banks, net	(569,762,669)	426,862,028
Unsecured loan repaid to banks	(500,000,000)	500,000,000
Unsecured loan received from director	63,615,000	561,441,959
Unsecured loan repaid to director	(231,180,073)	(84,850,957)
Unsecured loan repaid to others	(1,141,600)	(1,141,600)
Interest on loans	(221,535,945)	(254,576,867)
Proceeds from issue of shares	-	2,279,998,900
Share issue expenses	-	(36,000,000)
Net cash generated from/ (used in) financing activities (C)	(1,460,005,287)	3,391,733,463
D) Net increase in cash and cash equivalents (A+B+C)	(537,913,980)	1,149,506,440
E) Cash and cash equivalents as at the beginning of the year *	1,423,356,636	273,850,196
F Cash and cash equivalents as at the end of the year (D+E)	885,442,656	1,423,356,636.

6.1 The AR submitted that the assessee had Rs.142.33 crores of opening cash and cash equivalents as the first day of the ay ie on 01.04.2010 , substantial of such sum came from cash-flow generated from / used in the financial activities, particularly from the proceeds of issue of shares, during the period ended 31.03.2009. Thus, he submitted that the assessee had sufficient non-interest bearing funds at its command to meet the impugned investments in subsidiary, for the work- in- progress and the loan and advances given to associated concerns. Apart from that, he relied on the following judgments / decisions.

- i) Madras High Court decision in Redington (India) Ltd v. Addl. CIT [TCA No.520 of 2016, dt.23.12.2016, wherein it is held that where there is no exempt income in relevant year, there cannot be a disallowance of expenditure u/s.14A to any assumed income.
- ii) The decision of Gujarat High Court in the case of CIT v. Raghuvir Synthetics Ltd (2013) 36 taxmann.com 275, wherein the High Court held that where huge funds were available without any interest liability with assessee and there was no evidence to hold that borrowed money was utilized for purposes of advance to its sister concerns, no disallowance of interest was warranted.

We heard the rival submissions. We hold that section 14A is applicable even where the motive in acquiring the shares was to obtain controlling interest in the companies. The question in this case is whether interest bearing borrowings was utilized to acquire shares in the company and in making the advances etc. The assessee's share capital as on 31.3 2010 was at Rs.9.16 crores (Last year (Ly)Rs.9.16 crores) . Its

Reserves & surplus as on 31.3.2010 was at Rs.469.71 crores (Ly Rs.429.2416 crores). Thus, it has Rs.478.87 crores of non- interest bearing funds. The impugned investments in the subsidiary during the year was at Rs14.00 crores, the increase in the closing work- in- progress was at Rs. 10,08,07,321 and the loan and advances given to associated concerns was at Rs.17.96 crores. Thus, the total of them was at Rs 42.04crores only, which is much lesser than the interest free funds available with the assessee. Further, its Loan funds , both secured and unsecured, as on 31.3 2010 was at Rs.192.65 (Ly Rs.313.60 crores). Thus, there is a reduction in its interest bearing loan by Rs.120.95 crores during the year. On such facts, the interest disallowance made by Assessing Officer on such issues are unwarranted and hence corresponding Revenue's appeal grounds are dismissed. The next issue is whether the interest disallowance made u/s. 14A rwr 8D2(iii)is justified . In this regard, we have already noted that the assessee made investments in its subsidiary, during the year, at Rs. 14 crore and hence it must have incurred certain indirect expenses as explained by the CIT(A) in his order. It is an undisputed fact that during the year the assessee has taken a decision to make an investment in the subsidiary. Therefore, the expenditure incurred for taking such decision would fall within the category of expenditure incurred for earning the exempt income as per Section 14A. Except the investment in subsidiary, there is no other investment. Therefore, for the purpose of computing the disallowance as per Rule 8D(2)(iii), the amount of average investment would be Rs.7 crores and hence the disallowance made

at 0.5% of the average amount of the current year investment of Rs.7 crores would be restricted to Rs.3,50,000/- only. To this extent, the disallowance is justified. Thus the corresponding assessee's ground fails.

07. On the disallowance of Professional expenses at Rs.2,59,47,337, the AR submitted that from the details furnished by it the AO observed that out of Rs.4,29,51,841/- incurred towards professional and consultancy expenditure, Rs.2,59,43,337/-, ie more than 50% of the expenses were, made on provisional bases for which no details were furnished; and that the assessee was unable to prove the genuineness of the expenditure and hence disallowed Rs.2,59,43,337/-. During the appeal proceedings, the appellant explained that the professional and consultancy charges at Rs.2,59,47,337 was payable to M/s. L. S. Cable Ltd, for rendering technical assistance for laying under-ground cable, as per mercantile system. Since the revenue was offered for taxation, as per matching principle, the expenditure relating to the revenue requires to be booked and accordingly, it is booked and furnished copies of invoices and payment details. The CIT(A) held that M/s L. S. Cable Ltd raised invoice on 26.04.2010 and correspondingly passed journal entries in the books of the assessee on 14.05.2010 as such the liability crystallised in succeeding year, hence the claim is contingent liability, therefore not deductible in this assessment year and upheld the disallowance. Seeking our attention to clause (iv) "Revenue recognition" under "significant accounting policies" to the Schedule to the accounts, which is extracted as under :

"(iv) Revenue recognition

Revenue front of goods is recognised on transfer of all significant risks and rewards of ownership to the buyer. The amount recognised as sale is exclusive of sales tax and net of trade discounts and sales returns, Sales are presented both gross and net of excise duty.

Revenues from long term contracts (erection and commissioning) are recognized based on the principles laid down in AS 7 - "Construction Contracts" on the percentage of completion method, in proportion that the contract costs incurred for work performed up to the reporting date bear to the estimated total contract costs. Contract revenue earned in excess of hi Iii rig has been reflected under "Other Current Assets" and billing ill excess of contract revenue has been reflected under "Current liabilities" in the balance sheet. Variation in contract work, claims and incentive payments are included to the extent that dicy have been agreed with the customer. Where the outcome of it contract cannot be estimated reliably, contract revenue is recognised to the extent that contract costs incurred will be recoverable. Contract costs arc recognised as exenses till the period in which they are incurred. When it is probable that the total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately. Liquidated damages / penalties are provided as per the contract terms wherever there is a delayed delivery attributable to the Company.

Interest is recognised using the time proportion basis taking into account the amount outstanding and the interest rate applicable."

The AR submitted that the assessee followed, % complete contract method, offered the corresponding revenue on matching principle and hence pleaded that the above expenditure has to be allowed. Per contra, the DR supported the order of the CIT(A).

We heard the rival submissions. The assessee has clearly made out a case in its favour and hence we direct the AO to allow this claim subject to the following verification . We find that since the AO disallowed

this expense at the threshold , he has not examined as to whether this professional expenses suffered TDS or not. Hence, the AO would re-examine this issue as per the requirements under sec 40 (a)(ia) and decide the year of allowance of this expenses in accordance with that provision, after affording due opportunity to the assessee. This issue is treated as allowed for statistical purpose.

08. In the result, the assessee's appeal is partly allowed and the Revenue's appeal is dismissed.

Order pronounced in the open court on 5th day of May , 2017.

Sd/-

(VIJAY PAL RAO)
JUDICIAL MEMBER

MCN*

Sd/-

(S. JAYARAMAN)
ACCOUNTANT MEMBER

Copy to:

1. The assessee
2. The Assessing Officer
3. The Commissioner of Income Tax
4. The Commissioner of Income Tax (A)
5. DR
6. GF, ITAT, Bangalore

By Order

Assistant Registrar