

IN THE INCOME TAX APPELLATE TRIBUNAL
“D” Bench, Mumbai
Before S/Shri B.R. Baskaran (AM) & Sandeep Gosain (JM)

I.T.A. No. 1501/Mum/2016 (Assessment Year 2011-12)

ITO 9(2)(4) Room No. 623 6 th Floor Aayakar Bhavan M.K. Road Mumbai-400 020. (Appellant)	Vs.	M/s. Edelweiss Commodities Services Ltd. Edelweiss House Off. CST Road, Kalina Mumbai-400 098. PAN : AAKCS7311R (Respondent)
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Assessee by	Shri Jitendra Jain & Shri Ravikant Pathak
Department by	Shri Ram Tiwari
Date of Hearing	2.4.2018
Date of Pronouncement	6.6.2018

ORDER

Per B.R. Baskaran (AM) :-

The appeal filed by the revenue is directed against the order dated 16-12-2015 passed by Ld CIT(A)-16, Mumbai and it relates to the assessment year 2011-12. The revenue is aggrieved by the decision of Ld CIT(A) in holding that the assessee is entitled to set off of brought forward losses as against the provisions of sec. 79 of the Act. The revenue is also aggrieved by the decision of Ld CIT(A) in holding that the interest income should be netted off against interest expenditure and hence interest income should not be assessed separately.

2. The facts relating to the first issue are discussed in brief. The assessee company was earlier known as “Comfort Projects Ltd”. The shareholders as on 01-04-2010 were:-

(a) Manish Parekh	-	1,500 shares	15%
(b) Hiten Parekh	-	1,500 shares	15%
(c) Nayan Parekh	-	2,000 shares	20%
(d) Arvind Desai	-	5,000 shares	50%
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		10,000 shares	100%
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During the year relevant to the assessment year 2011-12, the assessee company was acquired by M/s Edelweiss Trading and Holding Ltd, as a result of which there was a change in the shareholding pattern exceeding 51%.

3. The assessee company was having brought forward business losses pertaining to immediately preceding AY 2010-11. In the return of income, the assessee sought set off of brought forward losses of AY 2010-11 to the extent of Rs.61,39,706/-. The AO took the view that the assessee was not entitled to claim set off of brought forward losses, since the provisions of sec.79 prohibits such a set off when there was a change in shareholding exceeding 49%. The provisions of sec. 70 read as under:-

“Sec 79. Carry forward and set off of losses in the case of certain companies

Notwithstanding anything contained in this Chapter, where a change in shareholding has taken place in a previous year in the case of a company, not being a company in which the public are substantially interested, no loss incurred in any year prior to the previous year shall be carried forward and set off against the income of the previous year unless-

(a) on the last day of the previous year the shares of the company carrying not less than fifty- one per cent of the voting power were beneficially held by persons who beneficially held shares of the company carrying not less than fifty- one per cent of the voting power on the last day of the year or years in which the loss was incurred.

Provided that nothing contained in this section shall apply to a case where a change in the said voting power takes place in a previous year consequent upon the death of a shareholder or on account of transfer of shares by way of gift to any relative of the shareholder making such gift.”

4. The assessee contended that the provisions of sec.79 will not be applicable to a “company in which public are substantially interested”. It was claimed that M/s Edelweiss Trading and Holding Ltd (which acquired the shares of assessee-company) is a 100% subsidiary of M/s Edelweiss Financial Services Ltd, a listed company. Accordingly it was submitted that as per the definition of the expression “Company in which public are substantially interested” given in sec. 2(18)(b)(B)(c), the assessee company shall become a

company in which public are substantially interested. Accordingly it was submitted that the provisions of sec. 79 would not be applicable to the assessee. The AO was not convinced with the explanations of the assessee and accordingly disallowed the claim of set off of brought forward losses.

5. The Ld CIT(A) was convinced with the explanations of the assessee and accordingly directed the AO to allow set off of brought forward losses.

6. The Ld D.R submitted that the assessee company was not a company in which public are substantially interested at the time when it was acquired by M/s Edelweiss Trading and Holding Ltd. Only after the acquisition, the assessee company has become a company in which public are substantially interested. He submitted that the provisions of sec. 79 would be applicable to the facts of the present case, as the company was a company in which public are not substantially interested and it became so only after the change in shareholding.

7. On the contrary, the ld A.R reiterated the submissions made before the tax authorities. Referring to the provisions of Companies Act, sec. 2(18) of the Income tax Act, the Ld A.R submitted that the assessee company has become a company in which public are substantially interested, after its acquisition by M/s Edelweiss Trading and Holding Ltd and accordingly contended that the provisions of sec. 79 would not apply to it.

8. We have heard rival contentions and perused the record. For the sake of convenience, we extract below the provisions of sec. 79 again, at the cost of repetition:-

“Sec 79. Carry forward and set off of losses in the case of certain companies

Notwithstanding anything contained in this Chapter, where a change in shareholding has taken place in a previous year in the case of a company, not being a company in which the public are substantially interested, no loss incurred in any year prior to the previous year shall be carried forward and set off against the income of the previous year unless-

(a) on the last day of the previous year the shares of the company carrying not less than fifty- one per cent of the voting power were beneficially held by persons who beneficially held shares of the company carrying not less than fifty- one per cent of the voting power on the last day of the year or years in which the loss was incurred]

Provided that nothing contained in this section shall apply to a case where a change in the said voting power takes place in a previous year consequent upon the death of a shareholder or on account of transfer of shares by way of gift to any relative of the shareholder making such gift.”

9. We have carefully perused the provisions of sec. 79 of the Act, more particularly, the following expression used in sec. 79:-

“Notwithstanding anything contained in this Chapter, where a change in shareholding has taken place in a previous year in the case of a company, not being a company in which public are substantially interested....”

Under common parlance a company in which public are not substantially interest is referred to as “Closely held company”. Similarly a company in which public are substantially interested is referred to as “Widely held company”. We notice that the provisions of sec. 79 talks about a closely company, wherein a change in shareholding has taken place. If the company was a widely held company at the time when the change in shareholding has taken place, then the provisions of sec. 79 will not apply. On a careful reading of above said provisions, in our view, the provisions of sec. 79 shall apply only to those companies which fulfill following two conditions, viz.,

(a) a change in shareholding has taken place (exceeding 49%) and

(b) the company was a closely held company at the time when the change has taken place.

As stated earlier, in our view, the above said two conditions have to be examined at the time when the change in shareholding takes place.

10. Now analyzing the facts prevailing in the instant case, we notice that both the above said conditions are satisfied in the instant case, viz.,

- (a) a change in shareholding exceeding 49% has taken place, since the entire shareholding held by earlier shareholders was acquired by M/s Edelweiss Trading and Holding Ltd.
- (b) on the date of change, the assessee company was a closely held company.

11. If we look at the object of introducing sec. 79, we may notice that sec. 79 in Chapter VI of the Income tax Act was introduced as an anti-abuse provision, intended to curb tax payers' attempt at transferring losses incurred by a corporate entity by means of transfer of shareholding. Hence this section restricts carry forward and set off of losses in the hands of closely held company (i.e., company in which public are NOT substantially interested), if the shares carrying atleast 51% of voting power are not beneficially held by persons who beneficially held such shares on the last date of the previous year in which the loss was incurred. The provisions of sec. 79 was not made applicable to widely held company (i.e., companies in which public are substantially interested).

12. Viewed from the object of introducing the provisions of sec. 79 of the Act, we may notice that the status of company at the time when the change in shareholding pattern takes place is relevant to determine the applicability of provisions of sec. 79 of the Act, i.e., whether it is a closely held company or widely held company at the time when the change in shareholding pattern takes place. If it is a closely held company at that point of time, then the provisions of sec 79 would apply and if it is a widely held company at that point of time, the provisions of sec. 79 will not apply. Hence the status of the company after the change in shareholding pattern is not relevant, i.e., even if the company becomes a widely held company, i.e., a company in which public are substantially interested, after the change in shareholding, even then the provisions of sec.79 would apply, if it was a closely held company at the time when change in shareholding takes place.

13. In the instant case, the assessee company was a closely held company at the time when the change in shareholding took place. It has become widely

held company after the change in shareholding. We have held that the status of company has to be examined at the time when the change in shareholding takes place. In the instant case, the status of the company was “closely held company”, i.e., a company in which public is not substantially interested, when the change in shareholding took place. Hence, we are of the view that the provisions of sec. 79 would apply to the company. Since there is a change in shareholding exceeding 49%, the assessee company is not entitled to set off brought forward losses relating to AY 2010-11 and earlier years.

14. In view of the foregoing discussions, we set aside the order passed by Ld CIT(A) on this issue and restore the order passed by the AO on this issue.

15. The next issue contested by the revenue relates to the interest income of Rs.4,74,658/- assessed by the AO as income from other sources, which has been deleted by the AO. The AO noticed that the assessee has received interest income of Rs.4,74,658/- from ICICI Bank and did not offer the same as income. When enquired, the assessee submitted that the above said interest income has been credited to Capital work in progress account. It was submitted that the assessee had borrowed money for building its corporate office and the interest expenditure was also capitalized. Accordingly interest income earned on the deposits kept as F.D with ICICI was credited to Capital Work in progress account. The AO did not accept the same and accordingly assessed the above said amount of Rs.4,74,658/- as income of the assessee under the head Income from other sources.

16. Before Ld CIT(A), the assessee furnished detailed explanations. It was submitted that the assessee obtained Letter of Credit facility from ICICI Bank in connection with the import of two quantity of air cooled remote radiator type DG sets from a Singapore company. As per the terms of the bank to give Letter of Credit facility, the assessee has made deposits with ICICI Bank. It was stated that the assessee had availed loan of Rs.360/- crores from its holding company named M/s Edelweiss Trading and Holding Ltd for construction of Corporate house and has paid interest of Rs.1267.47 lakhs on the said loan.

It was submitted that the above said interest expenditure was also capitalized. It was submitted that a part of loan funds were parked with ICICI Bank as Fixed Deposit for availing Letter of Credit facility for importing DG sets for the new building constructed by the assessee. Accordingly it was submitted that the interest income should be reduced from Capital work in progress as per the decision rendered by Hon'ble Supreme Court in the case of Karnal Co-operative Sugar Mills Ltd (243 ITR 2) and Bokaro Steels Ltd (236 ITR 315).

17. The Ld CIT(A) was convinced with the contentions of the assessee and accordingly directed the AO to delete the addition of interest income of Rs.4,74,658/-. The revenue is aggrieved by the decision of Ld CIT(A).

18. We heard rival contentions on this issue and perused the record. We notice that the Ld CIT(A) has examined the submissions made by the assessee that the fixed deposits have been kept with ICICI Bank in connection with the L/C facility availed by the assessee for import of DG sets for the corporate office constructed by the assessee. The assessee has furnished relevant documents before the Ld CIT(A). It is an admitted fact that the expenditure incurred in construction of corporate office has been shown as work in progress. The interest paid on loan taken for the purpose of construction of corporate officer has also been capitalized under the head "Capital Work in Progress". The assessee has imported DG sets from Singapore for the use of corporate office only. The assessee has made the fixed deposits out of loan funds with ICICI Bank for availing L/C facility for importing the DG sets only. Under these set of facts, there is link between the fixed deposits and the Corporate office constructed by the assessee. Hence the decision rendered by Hon'ble Supreme Court in the case of Karnal Co-operative Sugar Mills Ltd (supra) and Bokaro Steels Ltd (supra) shall apply to the facts of the case. Hence the assessee was justified in reducing the interest income from the above said fixed deposit from Capital work in progress. Accordingly we are of the view that the Ld CIT(A) has rightly directed the AO to delete the addition of interest income under the head income from other sources. Accordingly we uphold the order passed by Ld CIT(A) on this issue.

19. In the result, the appeal filed by the revenue is partly allowed.

Order has been pronounced in the Court on 6.6.2018.

Sd/-
(SANDEEP GOSAIN)
JUDICIAL MEMBER

Sd/-
(B.R.BASKARAN)
ACCOUNTANT MEMBER

Mumbai; Dated : 6/6/2018

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.

//True Copy//

BY ORDER,

(Senior Private Secretary)
ITAT, Mumbai

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