

IN THE INCOME TAX APPELLATE TRIBUNAL “A” BENCH : KOLKATA

[Before Hon’ble Shri Aby. T. Varkey, JM & Shri M.Balaganesh, AM]

I.T.A No. 750/Kol/2015

Assessment Years : 2009-10

M/s Titagarh Wagons Ltd.
[PAN: AABCT 1377 P]
(Appellant)

-vs-

ACIT, Range-1, Kolkata

(Respondent)

For the Appellant : Shri S.Jhajharia, FCA

For the Respondent : Shri P. K. Srihari, CIT(DR)

Date of Hearing : 05.07.2018

Date of Pronouncement : 11.07.2018

ORDER

Per M.Balaganesh, AM

1. This appeal by the Assessee arises out of the order of the Learned Commissioner of Income Tax(Appeals)-23, Kolkata [in short the Id CIT(A)] in Appeal No. 04/CIT(A)-23/Cir-1/LTU/14-15/Kol dated 24.03.2015 against the order passed by the ACIT, Circle-1, Kolkata [in short the Id AO] under section 143(3) of the Income Tax Act, 1961 (in short “the Act”) dated 26.12.2011 for the Assessment Year 2009-10.

2. The Id AR during the course of hearing stated that Ground Nos. 1 & 2 raised by the assessee are not pressed. The same is reckoned as a statement from the Bar and accordingly the Ground Nos. 1 & 2 are dismissed as not pressed.

3. The first issue to be decided in this appeal is as to whether the Id CITA was justified in upholding the disallowance made in the sum of Rs 1,34,81,243/- towards advances written off in the facts and circumstances of the case. The Id AR stated that the correct figure of disallowance should be considered at Rs 1,34,81,243/- as against Rs 1,14,81,243/- wrongly stated in the grounds of appeal. This typographical error is condoned and is taken up for adjudication.

3.1. The brief facts of this issue are that the assessee is a public limited company engaged in manufacturing of railway wagons and other allied items. The return of income for the Asst Year 2009-10 was filed by the assessee company on 23.9.2009 declaring total income of Rs 89,45,11,124/- . The Id AO observed that the assessee had written off certain advances in its books and claimed the same as deduction in the return of income in the sum of Rs 1,34,81,243/-. The break up of the same is as under:-

A) Vendor advances written off	- Rs 79,78,003
B) Vendor Advances written off (for past 4 -5 years)	- Rs 35,57,190
C) Earnest Money Forfeited by Customers	- Rs 19,46,050

TOTAL	Rs 1,34,81,243

The assessee gave the party wise break up of the aforesaid advances which were treated as irrecoverable and written off in the books of accounts. The Id AO observed that the assessee had not offered any income in respect of these advances either in the year under consideration or in the earlier years in terms of section 36(2) of the Act and accordingly the claim of the assessee of write off u/s 36(1)(vii) towards Bad debts is not sustainable. He also observed that the sid transactions pertain to earlier years and hence the same would also fall under the category of prior period expenses which cannot be allowed as deduction. The Id CITA upheld the action of the Id AO on the ground that though the details of various advances written off were furnished, but no supporting

evidences to that effect were furnished by the assessee. Hence the business nexus of those advances could not be established by the assessee.

3.2. Aggrieved, the assessee is in appeal before us.

3.3. We have heard the rival submissions. We find that the assessee had merely furnished the details of various advances given by it which were sought to be written off by it as irrecoverable and accordingly the same were claimed as deduction u/s 28 of the Act. But no supporting evidences were furnished in support of the details furnished by the assessee. The Id AR prayed before us for one more opportunity before the Id AO for furnishing the supporting evidences and for proving the business nexus of various advances and deposits given by the assessee which were sought to be written off together with the reasons for writing off the same. In response to this, the Id DR vehemently argued that the assessee had not complied with the provisions of section 36(2) of the Act in respect of these advances and hence the claim of the assessee u/s 36(1)(vii) of the Act should not be entertained. We find from the records that the assessee had used the nomenclature 'Debts and irrecoverable balances etc written off' in its profit and loss account. This admittedly contains bad debts written off u/s 36(1)(vii) of the Act to the tune of Rs 3,14,77,201/- which was originally disallowed by the Id AO in the assessment but was later allowed by the Id CITA. With regard to write off of irrecoverable advances, we find that the assessee had not made any claim u/s 36(1)(vii) of the Act for the same and hence the argument of the Id DR that assessee had not complied with provisions of section 36(1)(vii) read with section 36(2) of the Act has absolutely no basis at all. In our considered opinion, the duty is cast on the assessee to prove (i) that the advances were given in the normal course of its business thereby proving the business nexus; (ii) that the said advances had become irrecoverable due to various reasons; (iii) that the assessee had taken enough precautions and measures to recover the said advances but all their efforts were in vain

and (iv) accordingly the assessee chose to write off those advances in its books of accounts and claim the same as deduction u/s 28 of the Act. If these conditions are satisfied, then the assessee would be eligible for deduction u/s 28 of the Act in respect of irrecoverable advances written off. But there is no finding on facts with regard to these aspects in the orders of the lower authorities. In our considered opinion, the various case laws relied upon by the Id AR need not be considered at this stage without satisfying the aforesaid conditions on facts. Hence we deem it fit and appropriate in the interest of justice and fairplay, to remand this issue to the file of Id AO for de novo adjudication in accordance with law. The assessee is at liberty to adduce fresh evidences in support of its various contentions. Accordingly, the Ground Nos. 3 & 4 raised by the assessee are allowed for statistical purposes.

4. The next issue to be decided in this appeal is as to whether the Id CITA was justified in upholding the disallowance made u/s 14A of the Act read with Rule 8D of the Rules in the facts and circumstances of the case.

4.1. The brief facts of this issue are that the assessee had derived exempt income of Rs 3.60 crores in the form of dividend and claimed the same as exempt in the return of income. The assessee suo moto disallowed a sum of Rs 2,25,345/- u/s 14A of the Act in the return of income by applying the provisions of third limb of Rule 8D(2)(iii) of the Income Tax Rules, 1962. The Id AO observed that the assessee had paid interest on its borrowed funds to the tune of Rs 550.10 lakhs and accordingly in the proportion of total investments to the value of total assets, he worked out the disallowance of interest under Rule 8D(2)(ii) of the Rules and arrived at the disallowance figure of Rs 4,58,682/-. This action of the Id AO was upheld by the Id CITA. Aggrieved, the assessee is in appeal before us.

4.2. We have heard the rival submissions. We find that the assessee had made disallowance under third limb of Rule 8D(2) of the Rules in the sum of Rs 2,25,345/- which has been accepted by the Id AO as correct. We find that the assessee had claimed that there is no direct expenditure incurred for earning exempt income and accordingly no disallowance under the first limb of Rule 8D(2) is warranted, and this claim was also accepted by the Id AO. The only dispute is with regard to applicability of second limb of Rule 8D(2) of the Rules with regard to disallowance of interest. In this regard, the Id AR argued that the assessee on one hand paid interest to the tune of Rs 550.10 lakhs and on the other hand had earned interest income to the tune of Rs 1207.69 lakhs and hence once the same is netted with interest paid, there would be positive interest income only. Accordingly no disallowance under second limb of Rule 8D(2) of the Rules is warranted. Apart from this, he stated that the own funds available with the assessee company are several times more than the investments made and hence by placing reliance on the various decisions of Hon'ble Bombay High Court more particularly in the case of Reliance Utilities and Power Ltd reported in 313 ITR 340 (Bom), no disallowance of interest under second limb of Rule 8D(2) of the Rules is warranted. We find that the Id CITA had upheld the action of the Id AO by simply making a general finding that disallowance has been made in accordance with Rule 8D of the Rules. When the own funds are sufficiently available with the assessee which is staring on us on the face of the balance sheet, there cannot be any disallowance of interest on borrowed funds either u/s 36(1)(iii) or under second limb of Rule 8D(2) of the Rules. Hence by respectfully following the aforesaid decision of Hon'ble Bombay High Court among others, we direct the Id AO to delete the disallowance u/s 14A of the Act to the tune of Rs 4,58,682/-. Accordingly, the Ground No. 5 raised by the assessee is allowed.

5. The next issue to be decided in this appeal is as to whether the Id CITA was justified in upholding the disallowance of interest paid on borrowed funds u/s 36(1)(iii) of the Act in the facts and circumstances of the case.

4.1. The brief facts of this issue are that the Id AO observed that the assessee had advanced interest free loan to its Joint Venture M/s Cimco Equity Holding Pvt Ltd to the tune of Rs 22,50,00,000/-. He also observed that the assessee had advanced to its subsidiary company to the tune of Rs 36,95,00,000/- free of interest. Accordingly, he disallowed the interest paid on borrowed funds on a proportionate basis and arrived at the disallowance of interest in the sum of Rs 1,03,27,295/- u/s 36(1)(iii) of the Act by treating that these advances were diverted by the assessee for non-business purposes. The Id CITA observed that the advance to Joint Venture Cimco Equity Holding Pvt Ltd carried interest rate of 13.5% per annum and interest income offered accordingly by the assessee. To that extent, proportionately, the relief was granted by the Id CITA. With regard to disallowance of interest on amounts advanced to subsidiary company, the Id CITA upheld the action of the Id AO ignoring the various factual and legal submissions made by the assessee. Aggrieved, the assessee is in appeal before us.

4.2. We have heard the rival submissions. We find that the advances made to subsidiary company was only Rs 36.95 crores and whereas the own funds available with the assessee company in the form of share capital and reserves and surplus was Rs 391.03 crores. We have already held that when the own funds are sufficiently available with the assessee which is staring on us on the face of the balance sheet, there cannot be any disallowance of interest on borrowed funds u/s 36(1)(iii) of the Act. Moreover, it is not in dispute that the advances were made to subsidiary company only. We find that the purpose of lending is duly mentioned in the notes on accounts attached to the audited financial statements which are enclosed in pages 97 & 98 of the paper book. Hence the test of commercial expediency is proved beyond doubt. We find that the Hon'ble Apex

Court in the case of Hero Cycles P Ltd vs CIT reported in 379 ITR 347 (SC) had upheld our view and hence respectfully following the said decision and the decision of Hon'ble Bombay High Court in the case of Reliance Utilities and Power Ltd reported in 313 ITR 340 (SC), we direct the Id AO to delete the proportionate disallowance of interest on amounts advanced to subsidiary company. Accordingly, the Ground No. 6 raised by the assessee is allowed.

5. The final issue to be decided in this appeal is as to whether the Id CITA was justified in upholding the proportionate disallowance of interest paid in the sum of Rs 27,39,600/- on borrowed funds utilized for capital work in progress and capital expenditure on expansion , in the facts and circumstances of the case.

5.1. The brief facts of this issue are that the Id AO observed that the assessee has shown investment in capital work in progress including capital advances to the extent of Rs 4.18 crores as on 31.3.2009 and similarly investment on account of capital expenditure on expansion projects is found at Rs 11.58 crores as on 31.3.2009. The assessee submitted that these sums were incurred in connection with expansion of EMU Manufacturing Facility under construction. It was pleaded by the assessee that the entire investment made in EMU manufacturing facility has been sources out of proceeds of the public issue which are also reflected in page 45 of the annual report filed along with the return of income in the notes on accounts. The Id AO however observed that since this new unit has not commenced operations, the proportionate interest upto the date of installation requires to be capitalized in accordance with proviso to section 36(1)(iii) of the Act, which was not done by the assessee. Accordingly, he worked out the proportionate disallowance thereon and arrived at the disallowance figure of Rs 27,39,600/- in the assessment. The Id AO's primary assumption in this regard was that the assessee had paid interest on the borrowed funds and as such the said borrowed funds could have also been utilized for the purpose of

this expansion project and accordingly interest upto 31.3.2009 proportionately need to be capitalized to the said project which was not done by the assessee and accordingly requires to be disallowed. This action of the Id AO was upheld by the Id CITA. Aggrieved, the assessee is in appeal before us.

5.2. We have heard the rival submissions. We find that in the notes on accounts to the audited financial statements as on 31.3.2009, the assessee had stated as under:-

20. Details of utilization of Rs 11167.80 lacs raised through public issue till March 31, 2009 :

<u>Description</u>	<u>Estimated amounts to be Financed through issue Proceeds</u>	<u>Amounts Utilised till March 31, 2009</u>
<u>(Rs in lacs)</u>		
<i>EMU Manufacturing Facility</i>	1874.10	1576.45
<i>Upgradation of existing facilities and Sub-station</i>	1884.30	1884.30
<i>Wheel Assembly Plant</i>	1293.30	-
<i>Corporate Office</i>	700.00	251.17
<i>Strategic Acquisition</i>	1250.00	1250.00
<i>Brand Building Exercise</i>	200.00	22.55
<i>General Corporate Purposes</i>	3115.10	3115.10
<i>Issue Expenses</i>	851.00	851.00
	----- 11167.80	----- 8950.57
<i>Balance unspent money lying in short Term fixed deposits</i>	-	2217.23
TOTAL	----- 11167.80 -----	----- 11167.80 -----

Hence it could be seen that the total investment of Rs 4.18 crores and Rs 11.58 crores totaling to Rs 15.76 crores towards investment in EMU manufacturing facility and

capital expansion , a sum of Rs 11.17 crores is met out of proceeds of public issue which has got no cost. Hence there cannot be any interest attributable to the same. However, for the remaining investment of Rs 4.59 crores, the same should have been met only out of other own funds or out of borrowed funds. We have already held that the assessee had sufficient own funds at its kitty which are substantially more than the deficit herein of Rs 4.59 crores. Hence we hold that the remaining investment is also made only out of own funds of the assessee and hence there is no need for interest allocation to the cost of capital projects herein and accordingly no capitalization of interest is to be made as alleged by the Id AO. We find that the Id AO had not brought any nexus on record to prove that the borrowed funds were utilized for the purpose of capital expansion projects. Even otherwise, we find that the assessee had also earned interest income on its fixed deposits and loans and advances which is much more than the total interest claimed as deduction in the return of income. Hence in any case, there cannot be any disallowance of interest. Accordingly, the Ground No. 7 raised by the assessee is allowed.

6. The Ground No. 8 raised by the assessee is general in nature and does not require any specific adjudication.

7. In the result, the appeal of the assessee is partly allowed for statistical purposes.

Order pronounced in the Court on 11.07.2018

Sd/-
[A.T. Varkey]
Judicial Member

Sd/-
[M.Balaganesh]
Accountant Member

Dated : 11.07.2018

SB, Sr. PS

Copy of the order forwarded to:

1. M/s Titagarh Wagons Ltd., C/o, Salarpuria Jajodia & Co., 7, C.R. Avenue, Kolkata-700072.
2. Addl. CIT, Range-1, Kolkata, 'Aayakar Bhawan', P-7, Chowringhee Square, Kolkata-700069.
3. C.I.T(A)-
4. C.I.T.- Kolkata.
5. CIT(DR), Kolkata Benches, Kolkata.

True copy

By Order

Senior Private Secretary
Head of Office/D.D.O., ITAT, Kolkata Benches