

IN THE INCOME TAX APPELLATE TRIBUNAL
“C” BENCH : BANGALORE

BEFORE SHRI N.V. VASUDEVAN, VICE PRESIDENT
AND SHRI JASON P. BOAZ, ACCOUNTANT MEMBER

ITA Nos.333 to 339/Bang/2017
Assessment years : 2007-08 to 2013-14

Golflinks Software Park (P) Ltd., 1 st Floor, Embassy Point, 150, Infantry Road, Bangalore – 560 001. PAN: AABCG 7106K	Vs.	The Deputy Commissioner of Income Tax, Circle 11(3), Bangalore
APPELLANT		RESPONDENT

IT(TP)A No.384/Bang/2017
Assessment year : 2013-14

The Assistant Commissioner of Income Tax, Circle 3(1)(2), Bangalore.	Vs.	Golflinks Software Park (P) Ltd., Bangalore – 560 001. PAN: AABCG 7106K
APPELLANT		RESPONDENT

Revenue by	:	Shri Pradeep Kumar, CIT(DR)(ITAT), Bengaluru.
Assessee by	:	Shri G. Sitaram, CA

Date of hearing	:	06.05.2019
Date of Pronouncement	:	10.05.2019

ORDER

Per N V Vasudevan, Vice President

ITA No.333/Bang/2017

This appeal by the assessee is against the order dated 30.11.2016 of the CIT(Appeals)-3, Bengaluru relating to assessment year 2007-08.

2. There are basically two issues raised by the assessee in this appeal viz., disallowance of interest of Rs.47,62,545 u/s. 36(1)(iii) of the Income-Tax Act, 1961 [“the Act”] and another addition of Rs.1,00,20,000 being interest receivable from M/s. RPG Capital & Credits Ltd. [“**RPG**”].

3. As far as the first issue is concerned, the facts are that the assessee is a company engaged in the business of real estate development. In the course of u/s. 143(3) of the Act, the AO noticed that the assessee had advanced interest free loan of Rs.63,50,06,012 as on 31.3.2007 to M/s. Dynasty Developers Pvt. Ltd., [“**DDPL**”]. DDPL is a company in which the directors of the assessee have substantial interest. The assessee did not charge any interest on the sum advanced to DDPL. The AO noticed that the assessee availed of loans of Rs.578,46,86,896 from HDFC Bank and paid interest on such loans. The AO also found that the monies that were received as advance from HDFC Bank were transferred to DDPL.

4. The provisions of Sec.36(1)(iii) of the Act, reads as follows:

“36. (1) The deductions provided for in the following clauses shall be allowed in respect of the matters dealt with therein, in computing the income referred to in section 28—

.....

(iii) the amount of the interest paid in respect of capital borrowed for the purposes of the business or profession :

Provided that any amount of the interest paid, in respect of capital borrowed for acquisition of an asset for extension of existing business or profession (whether capitalised in the books of account or not); for any period beginning from the date on which the capital was borrowed for acquisition of the asset till the date on which such asset was first put to use, shall not be allowed as deduction.”

5. Thus, for allowance of a claim for deduction of interest under this provision following three conditions are required to be satisfied viz., (i) The money, that is capital, must have been borrowed by the assessee; (ii) It must have been borrowed for the purpose of business. (iii) The assessee must have paid interest on the borrowed amount i.e. he has shown the same as an item of expenditure. If the borrowed funds are not used for the purpose of business but are used for giving loans/advances to sister concern or third parties, then the interest expenditure to the extent borrowed funds are diverted for non business purposes, will not satisfy the test of "borrowed for the purpose of business of the Assessee" and interest expenditure will not be allowed as a deduction. The law on this issue is settled after the Hon'ble Supreme Court judgment in the case of S. A. Builders Ltd. v. CIT (Appeals) [2007] 288 ITR 1 (SC), in which the concept of "commercial expediency" was used. Thus, where the funds of the business are diverted for interest free loans the main criteria for permissibility of interest on those funds are based on whether it was for commercial expediency or not. The phrase "commercial expediency" has following important traits as purpose as is expected by the assessee to advance its business interest. It may include measures taken for preservation, protection or advancement of its business interests. It has however to be distinguished from the personal interest of its directors or partners, as the case may be. There has to be a nexus between the advancing of funds and business interest of the assessee. Some business objective should be sought to have been achieved by extending such interest free advances when the assessee-firm/company itself is borrowing funds for running its business. The Hon'ble Supreme Court has also delved into the case where there would be mixed fund at the disposal of the assessee. It further clarifies that under Section 36(1)(iii) the ultimate use of the

fund is important. It may not be relevant as to whether the advances have been extended out of the borrowed funds or out of mixed funds which include borrowed funds. The test to be applied in such cases is not the source of the funds but the purpose for which the advances are extended. The above principles has also been reiterated by the Hon'ble Supreme Court Hero Cycles (P) Ltd. Vs. CIT (Central, Ludhiana, Civil Appeal No.514 of 2008 dated 5.11.2015.

6. In the present case, as we have already seen borrowed funds on which interest was paid and which was claimed as deduction while computing income from business had been used to the extent of RS.63,50,06,102/- for giving interest free loan to DDPL. In the above circumstances, the AO was of the view that interest expenses claimed as deduction while computing income from business, on loans from HDFC Bank as a deduction should be disallowed to the extent of 9% of the amount advanced to DDPL of Rs. 63,50,06,012 on the ground that the loans on which interest was paid was not used for the purpose of business of the assessee and therefore the condition for granting interest expenditure as a deduction u/s. 36(1)(iii) has not been satisfied.

7. In reply to the aforesaid query of the AO, the assessee submitted that the loan in question was given by HDFC Bank as a commercial loan which could be used for any purpose. The assessee submitted that interest free advances given to the assessee's sister concern, DDPL, has to be considered as utilization of loans for the purpose of business. In this regard, the assessee submitted that it was in the business of real estate and the sum in question was given to DDPL for procuring property. Hence the interest free loan given to DDPL was for the purpose of business and

therefore no disallowance of interest as proposed by the AO could be made.

8. The AO called upon the assessee to furnish corroborative evidence to show that advances were given to DDPL for procurement of property. The assessee filed a letter dated 1.4.2003 from DDPL wherein there is a reference to arrangement for purchase of 9 acres of land at Kadubeesanahalli, Bangalore. The AO was of the view that but for the aforesaid letter, no other evidence was produced to show whether subsequently the property was registered in assessee's name in subsequent assessment years. In these circumstances, the AO disallowed a sum of Rs.47,62,545 [9% of 63,50,06,012] out of interest expenses claimed as deduction by the assessee.

9. Aggrieved by the aforesaid addition made by the AO, the assessee preferred appeal before the CIT(Appeals).

10. Even before the CIT(Appeals), the assessee did not produce any evidence to substantiate its case of advance to sister concern – DDPL, being for business purposes. The CIT(Appeals), therefore, held that merely because both the assessee and its sister concern are engaged in real estate business, there cannot be a presumption that the money advanced to DDPL was for the purpose of business of the assessee. Before the CIT(Appeals), the assessee had also taken a plea that funds on which interest was paid and which was claimed as deduction in the P&L account were not used for the purpose of making advances to DDPL. The assessee had claimed that it had non-interest bearing funds of Rs.288.97 crores including sundry creditors which was utilised for advancing money to DDPL. This plea was also not substantiated with sufficient evidence.

Therefore, the claim of the assessee on this basis was also rejected by the CIT(Appeals). Aggrieved, the assessee is in appeal before the Tribunal.

11. The Id. counsel for the assessee drew our attention to the balance sheet & P&L account of assessee as on 31.3.2007 and Note 16 of the Notes to Accounts, wherein there is a reference to the assessee having paid a sum of Rs.99,87,30,918 as business consultancy services remuneration to DDPL. Our attention was also drawn to the fact that the assessee had incurred certain expenses on behalf of DDPL and those were reimbursed to the extent of Rs.20,41,328. In the above circumstances, it was submitted that there was a business connection between the assessee and DDPL. Therefore, it should be presumed that interest free loan was given owing to commercial expediency. It was also submitted that the CIT(Appeals) in confirming the order of the AO, has made a reference to the decision of the Hon'ble High Court of Karnataka in the case of ***Embassy Development Corporation v. ACIT [2015] 52 taxmann.com 234***, wherein it was held that there was no business expediency in advancing loans to sister concern on identical facts as in the case of the Assessee in this appeal. In the aforesaid case, the assessee as well as its sister concern were engaged in real estate business. Money was advanced to the sister concern out of borrowed funds for the purpose of acquiring part of property which was to be developed by the sister concern. Even after 3 years, no such purchase was made. In these circumstances, it was held that the amounts borrowed were not utilised for the purpose of business of assessee. According to the Id. counsel for the assessee, the aforesaid decision is distinguishable for the reason that there was no evidence of property not having been purchased by the sister concern i.e., DDPL in the present case.

12. The Id. DR relied on the order of CIT(Appeals).

13. We have considered the rival submissions and are of the view that the plea put forth by the Id. counsel for the assessee cannot be accepted. As rightly held by the CIT(Appeals), there was no business purpose established by the assessee for which advances were given to DDPL. The claim of assessee that advances were given for purchase of property by the sister concern has not been established. Moreover, from the fact that assessee and sister concern were both in real estate business, advances given by one to the other cannot be treated as for business purpose, unless evidence is let in to show expenses of business purpose. Even before us, the plea of existence of own funds out of which interest free advances were given to sister concern has also not been established. The argument of the learned counsel for the Assessee that in the present case there is no evidence to show that properties were not purchased by DDPL in the present case cannot be the basis to distinguish the decision of the Hon'ble Karnataka High Court in the case of Embassy Development Corporation (supra). The Assessee is claiming deduction of interest expenditure and it is for the Assessee to establish that borrowed funds on which interest was paid and which is claimed as deduction in computing income from business is in fact used for the purpose of business. In these circumstances, we uphold the order of CIT(Appeals) and find no merits in the first issue raised by the assessee.

14. The second issue that arises for consideration is with regard to addition of Rs.1,00,20,000/- on account of interest receivable from RPG. The facts in this regard are that the assessee had given an advance of Rs.16 crores to RPG by way of Inter-Corporate Deposits ["ICDs"]. On such deposit, interest was payable by RPG. RPG had in its books of account debited interest expenses payable to assessee and had also made deduction of tax at source (TDS). Though RPG had not paid interest to the

Assessee, yet it had in its books recognized liability. Under the mercantile system of accounting followed by the Assessee, right to receive income will be sufficient to construe accrual of income. In these circumstances, the interest income that accrued to the assessee which ought to have been declared by the assessee and which was not declared in the return of income by the Assessee was brought to tax by the AO. The above information of credit of interest by RPG came to the knowledge of AO through AIR information.

15. Before the CIT(Appeals), the assessee submitted that the aforesaid AIR information was not brought to the notice of assessee by the AO in the course of assessment proceedings. However, the assessee did not furnish any specific explanation as to why the interest income should not be brought to tax on accrual basis in the hands of assessee. Aggrieved by the order of CIT(A), the assessee is in appeal before the Tribunal.

16. The Id. counsel for the assessee submitted before us that the sum of Rs.16 crores due and payable by RPG had been assigned to M/s. More Finance Share Investments Pvt. Ltd. as early as in AY 2005-06 and in such circumstances, the interest income in question cannot be brought to tax in the hands of assessee. We have considered the submissions and are of the view that no such plea was put forth before the lower authorities. Even before us, no evidence has been let in to substantiate the claim of assessee with regard to assignment of ICDs by the assessee to a third party. In these circumstances, we find no merit in the relevant grounds of appeal of the assessee. Accordingly, the second issue is also decided against the assessee.

17. In the result, the assessee's appeal is dismissed.

ITA No.334/Bang/2017

18. This appeal by the assessee is against the order dated 30.11.2016 of the CIT(Appeals)-3, Bengaluru relating to assessment year 2008-09.

19. In this appeal, two issues arise for consideration viz., (1) disallowance of interest on advances made to DDPL of Rs.3,50,42,297 and disallowance of interest on interest-free loans to Topaz Investments Pvt. Ltd. [“**TIPL**”] of Rs.72,36,903. Both the aforesaid disallowance of interest are u/s.36(1)(iii) of the Act and (2) disallowance u/s. 14A of the Act of Rs.2,32,511.

20. The second issue was not pressed for adjudication and the same is dismissed as not pressed.

21. On the first issue, as far as disallowance u/s. 36(1)(iii) of the Act on account of borrowed funds which were diverted as interest-free loans to DDPL is concerned, the facts are identical to the facts as it prevailed for AY 2007-08. Even in this assessment year, the assessee has not been able to establish that interest-free loans to sister concern was for the purpose of business of the assessee or owing to commercial expediency. In these circumstances, we find no merit in the grounds of appeal raised by the assessee.

22. As regards disallowance of interest u/s. 36(1)(iii) of the Act on the ground that interest bearing loans were used to give interest-free funds to TIPL of Rs.72,36,903, the facts are identical to the facts as it prevailed for the AY 2007-08 wherein a similar disallowance was made in the case of assessee, in proceedings u/s. 148 of the Act. The disallowance for interest paid to DDPL which was subject matter of discussion in ITA No.333/Bang/2017 was also made for the same AY 2007-08 but that was in

the proceedings u/s. 143(3) of the Act. The disallowance of interest paid to TIPL was subject matter of an appeal by the assessee before the Tribunal in ITA No.332/Bang/2017 for the AY 2007-08 and this Tribunal by its order dated 15.02.2019 came to the conclusion that the matter has to be remanded to the CIT(Appeals) for fresh consideration. Before the Tribunal, the assessee has submitted rental income due to the assessee every month was transferred as advance to TIPL and borrowed funds on which interest was paid was not utilized to give interest free loans to TIPL. The further submission was that advances were given for purchase of land. The Tribunal, after taking note of the above submissions came to the following conclusion:-

“11. We have heard the rival contentions and perused the record. We notice that the Ld CIT(A) has taken support of the decision rendered by the Hon’ble Karnataka High Court in the case of Embassy Development Corporation (supra) to uphold the addition made by the AO, since, according to Ld CIT(A), the assessee has failed to prove commercial considerations involved in giving such advances. By analyzing the financial statements, the Ld CIT(A) has taken the view that the assessee has diverted interest bearing funds for giving the impugned advances to M/s TIPL. Hence he has held that the interest attributable to the advances so given is not allowable as deduction. Hence, in our view, it is not a case of addition of Notional interest income. Before us, the assessee has not furnished the copies of financial statements and hence we are unable to appreciate the contention of the assessee. In addition to the above, the assessee has also furnished a copy of ledger account to submit that there are business dealings between the assessee and M/s TIPL. A perusal of the same would show that the assessee appears to have sold some properties to M/s TIPL and received money in instalments, while the issue before us is with regard to the advances given by the assessee to M/s TIPL. In any case, this ledger account copy and the nature of business transactions have not been examined by Ld CIT(A).

12. We also notice that there is lack of clarity on the facts surrounding the issue. The assessee claims that it has not diverted any loan funds for giving impugned advances and it has used only its rental income proceeds for giving the advances. However, the Ld CIT(A), after analyzing the financial statements of the assessee, has given a finding that the assessee does not possess interest free funds equivalent to or in excess of the advance given. The Ld A.R also submitted that the quantum of advance mentioned by the tax authorities is not correct.

13. In view of the above, we are of the opinion that this issue requires fresh examination at the end of Ld CIT(A) by providing one more opportunity to the assessee to substantiate its case. Accordingly we set aside the orders passed by Ld CIT(A) on this issue in all the three years under consideration and restore the same to the file of Ld CIT(A) for examining it afresh in accordance with law, after affording adequate opportunity of being heard to the assessee.

23. Following the aforesaid decision of the Tribunal, we remand the issue to the AO for fresh consideration as per the directions of the Tribunal referred to above and in the light of the conclusions that may be drawn in AY 2007-08.

24. In the result, the appeal of the assessee is treated as partly allowed for statistical purposes.

ITA No.335/Bang/2017

25. This appeal by the assessee is against the order dated 30.11.2016 of the CIT(Appeals)-3, Bengaluru relating to assessment year 2009-10.

26. There are basically two issues that arise for consideration in this appeal viz., disallowance of interest u/s. 36(1)(iii) of the Act on the ground that interest bearing funds were diverted to DDPL and TIPL being for non-business purposes and not having any commercial expediency. The facts

in connection with the aforesaid issue are identical to the facts as it prevailed in the case of assessee for AY 2007-08. For the reasons stated while deciding the issue of disallowance of interest u/s. 36(1)(iii) on loans advanced to DDPL, we confirm the order of CIT(Appeals).

27. In respect of disallowance of interest of advance to TIPL, the issue is remanded to the AO for fresh consideration as directed by the Tribunal for the AY 2007-08, which we have referred to in the earlier part of this order.

28. In the result, the appeal by the assessee is partly allowed for statistical purposes.

ITA No.336/Bang/2017

29. This appeal by the assessee is against the order dated 30.11.2016 of the CIT(Appeals)-3, Bengaluru relating to assessment year 2010-11.

30. As far as this appeal is concerned, there are basically three issues that arise for consideration. (i) The first issue is with regard to the computation of disallowance u/s. 14A of the Act r.w.s. Rule 8D(2)(iii) of the I.T. Rules while determining total income under the Normal Provisions of the Act. (ii) The second issue is with regard to disallowance of expenses incurred for the purpose of earning income which does not form part of total income under the Act under Chapter III of the Act while computing book profits for the purpose of levy of tax on book profits u/s.115JB of the Act. (iii) The third issue is with regard to deduction claimed by the assessee on account of capital advances written off of Rs.9,64,74,211 which was not allowed by the revenue authorities.

31. As far as the first and the second issue are concerned, the facts are that the assessee earned exempt income and therefore expenditure

incurred in earning exempt income should be disallowed and added to the total income of assessee as provided in section 14A of the Act. The expenditure to be disallowed u/s.14A of the Act in this case had to be worked out on the basis of Rule 8D(2)(ii) & (iii) of the Income Tax Act Rules, 1962 (Rules). There is no dispute on this aspect. Section 115JB of the Act provides that notwithstanding anything contained in any other provision of the Act, where in the case of an assessee, being a company, the income-tax, payable on the total income as computed under this Act in respect of any previous year relevant to the assessment year commencing on or after the 1st day of April,2007, is less than ten per cent of its book profit, such book profit shall be deemed to be the total income of the assessee and the tax payable by the assessee on such total income shall be the amount of income-tax at the rate of ten per cent. The Assessee being a company the provisions of Sec.115JB of the Act were applicable. Every assessee, being a company, shall, for the purposes of this section, prepare its profit and loss account for the relevant previous year in accordance with the provisions of Parts II and III of Schedule VI to the Companies Act, 1956 (1 of 1956). In so preparing its book of accounts including profit and loss account, the company shall adopt the same accounting policies, accounting stand and method and rates for calculating depreciation as is adopted while preparing its accounts that are laid before the company at its annual general meeting in accordance with provisions of Sec.210 of the Companies Act. Explanation below Sec.115JB of the Act provides that for the purposes of section 115JB of the Act, "book profit" means the net profit as shown in the profit and loss account for the relevant previous year prepared under sub-section (2), as increased by— certain items debited in the profit and loss account in arriving at the net profit and as reduced by- certain items that are credited in the profit and loss account. In other words, all that one has to do, while computing book profits is to

take the profit as per profit and loss account prepared in accordance with Companies Act, 1956 and make additions or subtraction as is given in the explanation to Sec.115JB(2) of the Act. One such addition to the profit as per profit and loss account provided in explanation to 115JB(2) is expenses incurred to earn income which is exempt under Chapter III of the Act. The AO added the sum determined as expenses to be disallowed u/s.14A of the Act while determining total income under the normal provisions of the Act also while determining the book profits u/s. 115JB of the Act which was a sum of Rs.45,46,667.

32. The disallowed u/s. 14A of the Act was arrived at by the AO in the following manner:-

A.	Total amount of Direct interest	NIL		
B.	Total amount of indirect interest pertaining to tax – exempt investments	99,81,70,460		
		AY 09-10	AY 10-11	Average
C.	Average amount of tax exempt investments	5,71,53,625	1,12,13,375	3,41,83,500
D.	Average amount of total assets	736,14.28.691	823,40,50,992	779,77,39,341
E.	Proportionate indirect interest to be disallowed	$\frac{B \times C}{D}$	$\frac{3,41,83,500 \times 99,81,70,460}{779,77,39,341}$ = 43,75,750	
F.	0.5% of average amount of tax exempt investments		1,70,917	
G	Total disallowance attracted u/s. 14A read with Rule 8D	A + E + F	45,46,667	

33. On appeal by the assessee, the CIT(Appeals) confirmed the order of AO.

34. It is the plea of the assessee before us that while applying the formula prescribed under Rule 8D(2)(ii) and (iii) and while computing the disallowance u/s. 14A of the Act and while determining total income of assessee under the normal provisions of the Act, the average value of investments should be worked out without including the investments which did not yield exempt income during the relevant previous year.

35. As far as the amount to be added to the profit as per P&L account u/s. 115JB of the Act is concerned towards expenditure incurred in earning income exempt u/s. Chapter III of the Act, the plea of the assessee was that the disallowance u/s. 14A of the Act made while computing total income under the normal provisions of the Act should not be automatically added while determining the book profits u/s. 115JB of the Act. In support of the stand taken by the assessee, the assessee has placed reliance on the decision of the Delhi Special Bench of ITAT in the case of *ACIT v. Vireet Investments Pvt. Ltd., 165 ITD 25 (Del)(SB)*. In the aforesaid decision, two questions were considered by the Special Bench which are as follows:-

“(i) Whether the expenditure incurred to earn exempt income computed u/s 14A could not be added while computing book profit u/s 115JB of the Act? And

(ii) Whether investments which did not yield any exempt income should enter into the computation under Rule 8D while arriving at the average value of investment, income from which does not form part of the total income?

36. The Special Bench answered the aforesaid questions as follows:-

“(i) We answer the question referred to us in favour of assessee by holding that the computation under clause (f) of Explanation 1 to section 115JB(2). is to be made without

resorting to the computation as contemplated u/s 14A read with Rule 8D of the Income-tax Rules, 1962.

(ii) Only those investments are to be considered for computing the average value of investment which yielded exempt income during the year.

37. In view of the aforesaid decision of the Special Bench, we direct the AO to compute the disallowance u/s. 14A of the Act while determining the total income under the normal provisions of the Act by taking into consideration only the investments which yielded exempt income for arriving at the average value of investments before applying the formula under Rule 8D of the Rules.

38. As far as the amount to be added while computing book profits u/s. 115JB of the Act is concerned, the AO cannot add the sum determined as disallowance u/s. 14A of the Act while computing total income under the normal provisions of the Act and he has to adopt a basis as laid down by the Special Bench in the aforesaid decision viz., direct expenditure associated with earning of income. We direct the AO to compute the disallowance u/s. 14A accordingly under the normal provisions of the Act as well as on the basis of book profits u/s.115JB of the Act.

39. The relevant grounds of appeal of assessee is treated as allowed for statistical purposes. Issue Nos.1 & 2 are decided accordingly.

40. As far as the third issue is concerned, the assessee claimed deduction of a sum of Rs.9,64,74,211 as impairment of capital advances. The claim of assessee in this regard was that advances given were not realizable and therefore it was decided to write off in the books of account in accordance with the Accounting Standards. When the AO called upon the assessee to justify the deduction on account of impairment of capital

advances, the assessee agreed before the AO that the said sum cannot be claimed as a deduction in accordance with law and accordingly the claim for deduction was disallowed by the AO with the following observations:-

“”20. Further it is noticed that the assessee company has debited an amount of Rs 9,64,74,211 as impairment of capital advances in P & L account. When this issue was brought to the notice of the assessee and its allowability under the provisions of Income tax Act as also the fact that it is was not added back in the computation of income filed by assessee.

i. The assessee has replied that " we would like to bring to your kind attention the fact that we have committed an error in computing the total income after ignorance of the fact that the impairment of assets are not allowable under the provisions of I T Act, and also we missed out this impairment amount of Rs 9,64,74,211 from our computation of income and when realizing this fact we decided to revise the return, however the prescribed time limit for revising the return has elapsed, therefore we are now bringing to your notice that the amount of Rs 9,64,74,211 to be added back to the returned income"

ii. The above submissions have been perused and examined. It is noted that the assessee company has accepted this fact and requested for adding back to total income, only after this lapse was pointed out by the Assessing Officer. After considering the above, I proceed to add back the amount of Rs 9,64,74,211 being impairments of assets to the returned income, and for this reason penalty proceedings u/s 271(1)(c) are initiated.”

41. Before the CIT(Appeals), the assessee submitted that while computing book profits u/s. 115JB of the Act, a sum of Rs.9,64,74,211 debited in the P& L a/c as impairment of capital advances and that cannot be added to the profit as per profit and loss account prepared in accordance with Companies Act, 1956, while computing book profit for the levy of tax on book profits u/s.115JB of the Act. The plea of the Assessee

was that AO cannot add to the profit as per profit and loss account prepared in accordance with Companies Act, 1956, any sum which does not fall within the ambit of any of the items of additions or exclusions as provided in Explanation to section 115JB(2) of the Act. The assessee placed reliance on the decision of the Hon'ble Supreme Court in the case of *Apollo Tyres Ltd. v. CIT, 255 ITR 273 (SC)* wherein the Hon'ble Supreme Court held that while calculating book profits u/s. 115JB of the Act, the AO cannot tinker with the P&L account, except to the extent permitted by the Explanation u/s. 115JB(2) of the Act. In other words, the profit as per P&L account prepared in accordance with the Companies Act, 1956 should be the starting point and exclusions & inclusions to the said profit to arrive at the book profits should be only on the basis of permissible items of inclusion & exclusion as provided under Explanation to section 115JB of the Act.

42. The CIT(Appeals) found that the claim of assessee was not legally correct for the reason that the Assessee on its own admitted that this item of expenditure is not admissible while computing income under the normal provisions of the Act. The following were the relevant observations of the CIT(A):-

“10.2 With regard to the addition of Rs.9,64,74,211/- made to the Book profit, it is relevant to note that the deduction of this amount in the Profit a Loss account was patently inadmissible. In fact during the assessment proceedings, the appellant has stated before the AO that it had committed an error in computing the total income due to ignorance of the fact that the impairment of asset is not allowable as deduction under the provisions of the Income Tax Act. This is specifically discussed in para 20 of the Assessment Order. Therefore, it is very much evident that the claim of deduction of this amount in the Profit Et Loss account was patently inadmissible as per the provisions of law. Therefore, the profit as shown in the P&L account should have been higher

by Rs.9,64,74,211/-, but for the wrong claim of deduction by the appellant. Therefore the addition of the corresponding amount for computing the Book profit is found to be legally correct and justified. The contention of the appellant against the addition of the sum of Rs.9,64,74,211/- to the Book profit is rejected. The grounds of appeal raised in this regard are accordingly, dismissed.”

43. Aggrieved by the order of CIT(Appeals), the assessee is in appeal before the Tribunal. We have considered the rival submissions. It is clear from the order of CIT(Appeals) that he has not addressed the issue raised by the assessee. He has proceeded on the basis that the deduction is claimed in computing total income as per the normal provisions of the Act. It is true that the Assessee agreed for addition of this sum to the total income while computing total income under the normal provisions of the Act, but while computing book profits u/s.115JB of the Act, the plea of the Assessee was that this sum is not one of the item to be added to the profit as per profit and loss account prepared in accordance with the provisions of Companies Act, 1956, as provided in Explanation to Sec.115JB(2) of the Act. Therefore the conclusions of the CIT(A) in this regard is incorrect because the claim of the Assessee is in the context of determination of book profits u/s. 115JB of the Act. It is clear from a reading of Explanation to section 115JB(2) of the Act that the amount debited in the P&L account towards impairment of capital advances was not an item which should be added back to the profit as per P&L account for arriving at the book profits. In the light of the decision of the Hon'ble Supreme Court in the case of *Apollo Tyres Ltd. (supra)*, the AO was therefore not competent to add the aforesaid sum to the profit as per P&L account while determining the book profits. We hold accordingly and allow the relevant ground of appeal of the assessee.

44. In the result, the appeal of the assessee is partly allowed.

ITA No.337/Bang/2017

45. This appeal by the assessee is against the order dated 30.11.2016 of the CIT(Appeals)-3, Bengaluru relating to assessment year 2011-12.

46. There are basically two issues that arise for consideration in this appeal, viz., disallowance of interest u/s. 36(1)(iii) of the Act of Rs.22,71,40,434 and disallowance of expenses u/s. 14A of Rs.53,553.

47. The issue with regard to disallowance of interest u/s. 14A of the Act was not pressed before us, hence the same is dismissed as not pressed.

48. As far as disallowance of interest u/s. 36(1)(iii) of the Act is concerned, the facts are that the Assessee had availed of secured loans of Rs 1035,81,74,018. The AO also noticed that the Assessee had given the following advances for the following purposes:

- a. a sum of Rs. 14,70,56,552 as loans to group companies;
- b. a sum of Rs 61,50,00,00 as advance for new ventures;
- c. a sum of Rs 146,49,22,969 as advance towards share application money.

The Assessee had paid interest of loans availed from financial institutions & banks and incurred interest expenses to the extent of Rs 137,83,92,147.

49. The AO called upon the Assessee to why interest expenditure debited to profit and loss account should not be disallowed proportionate to the extent the same was used for giving advances to sister concerns as detailed above, for the reason that interest expenditure to that extent cannot be regarded as expended wholly and exclusively for the purpose of assessee's business. In response the assessee's authorized representative claimed that the amounts were given for business purposes. However, the

assessee did not produce any evidence to show the business expediency or any direct nexus between the borrowed funds and the loans/advances given as stated above. The AO therefore disallowed interest expenditure to the extent of Rs 24,11,42,713 out of the interest expenditure claimed as deduction of Rs 112,16,08,065. against the House Property Income of the assessee for the said A. Y. under consideration. The interest allowable was worked out by the AO at Rs. 88,04,65,352 (Rs.112,16,08,065 – Rs.88,04,65,352) as follows:

$$\frac{112,16,08,065 \times 2226979521}{10358174018} = 24,11,42,713.$$

Rs.22,69,79,521 is the sum total of the three advances referred to in paragraph-47 of this order. Rs.1035,81,74,018 is the total advances taken by the Assessee from banks on which interest paid was Rs.112,16,08,065.

50. Before the CIT(A) the assessee that it made an advance of Rs.14.70 crores to group companies viz., M/s. D M Estates (P) Ltd., and M/s. GV Properties (P) Ltd. and an advance of Rs.61.50 Crores, M/s. Embassy Property Development (P) Limited (EPDPL) and submitted that these advances were made for business ventures and development of property. The Assessee submitted that all the entities to which the Assessee gave advances and the Assessee were engaged mainly in the business of land development and therefore, the advances made to these entities should be considered as advance made for the purpose of business. The CIT(A) held that the Assessee has not furnished any specific purpose for which money was advanced to the group companies as referred above. He held that the Assessee has not explained how such advances made to those companies complemented the business interest of the Assessee. According to CIT(A) the fact that all group companies are engaged in the real estate business cannot be the basis to infer that any

amount of money which is advanced to such companies would promote the interest of the Assessee. He held that without bringing on record the specific purpose for which the money was advanced to the group companies as referred above, it cannot be automatically accepted that the money was advanced and utilized for the company. He held that since it was undisputed that advances to sister concerns were made out of borrowed funds, the Assessee having failed to prove that the amounts advanced to the group concerns were out of the non-interest bearing funds of the Assessee, he held that disallowance of interest on the advances to group companies was valid.

51. With regard to advance of Rs.146,49,22,969/- for purchase of shares including share application money, the Assessee submitted that a sum of Rs.131,15,22,969/- was given towards share application money for acquiring shares of Umbel Properties (P,) Ltd (UPPL). The Assessee claimed that the investment in UPPL was for developing a big project in Bangalore. The Assessee claimed that it was one of the promoters of the said project and shares had been allotted to the Assessee in the subsequent year. The CIT(A) held that since the money was given for acquiring shares of another company, interest payable on such advance cannot be allowed as revenue expenditure. In this regard the CIT(A) relied on the decision of the Hon'ble Karnataka High Court in the case of *CIT Vs. LK Trust (2008) 297 1TR 53, (Karnataka)*, in which it was held that interest on money borrowed for acquiring shares where the assessee had borrowed money for investment in shares which was not in line with the business of the assessee, interest on such borrowings cannot be allowed as deduction from the business income. The CIT(A) also held that the claim of the Assessee that the amounts were advanced for business promotion and the funds have been fully utilized for the specified projects was not

proved by letting in any evidence except merely claiming that the money was advanced to UPPL as share application money for being invested in a big project in Bangalore in which the Assessee was one of the promoters.

52. The CIT(A) however found that the Assessee has received interest of Rs.1,75,48,359/- from the group companies in respect of the advances made. The CIT(A) found from financial statements that a sum of Rs.1,75,48,359/- was included under the head "Other income", which was evident from Note 13 in the Schedule to the Profit & Loss account. He also found that tax was deducted in respect of the said income. Accordingly, the CIT(A) held that to the extent of interest received on advances, the disallowance made by the AO should be deleted. The relevant findings of the CIT(A) in this regard was as follows:-

“7.1 From the financial statements for the year under consideration, it is observed that the appellant has received a sum of Rs.1,75,48,359/- towards interest on loans and securities given to companies. This is evident from the details furnished under "Other income" in Note 13 to the Schedule to the Profit a Loss account. In this regard the appellant has furnished the break up as per which it is observed that it has received a sum of Rs.80,66,146/- as interest from DM Estates (P) Ltd and GV Properties (P) Ltd and Rs.59,36,543/-as interest from other group companies. The appellant has also furnished details of the tax deducted at source in respect of the interest received from DM Estates (P) Ltd and GV Properties (P) Ltd. However the total amount of interest received from these two companies and other group companies is found to be only Rs.1,40,02,689/-. Therefore considering these facts it is very much evident that the appellant has received interest to the extent of Rs.1.40 crores from the group companies, as stated above. Accordingly the amount of interest disallowance determined by the AO should be reduced by the amount of interest received from these companies. The AO is directed accordingly. Therefore the disallowance of balance interest to the extent of Rs.22,71,40,024/- is confirmed. The

grounds of appeal raised in this regard are accordingly partly allowed.”

53. Aggrieved by the order of CIT(Appeals), the assessee has preferred the present appeal before the Tribunal. The Id. counsel for the assessee reiterated submissions made before CIT(A) with regard to advances made of Rs.14.70 crores to group companies viz., M/s. D M Estates (P) Ltd., and M/s. GV Properties (P) Ltd. and an advance of Rs.61.50 Crores, M/s. Embassy Property Development (P) Limited (EPDPL) We have already decided a similar issue in the AY 2007-08 and we have also referred to the decision of the Hon'ble High Court of Karnataka in the case of *Embassy Development Corporation (supra)* while deciding similar issue for AY 2007-08. We are of the view that in the light of absence of any evidence to show the purpose for which the loans/advances were given and their utilization, the revenue authorities were justified in disallowing interest u/s. 36(1)(iii) of the Act on the ground that borrowed funds on which interest was paid were given to sister concerns without charging any interest and were therefore not for the purpose of business of assessee.

54. As far as sum of Rs.146,49,22,969 is concerned, the plea of the Id. counsel for the assessee was that a sum of Rs.131,15,22,969 was share application money to acquire shares of UPPL for the purpose of developing of a big project. The assessee claimed that it was promoter of this company and was a major shareholder of the company. This claim of assessee was also rightly rejected by the revenue authorities for the reason that no evidence was let in to prove the commercial advantage that the assessee would receive by such investments or the business expediency of making the aforesaid investments. The CIT(Appeals) in this regard has rightly placed reliance on the decision of the Hon'ble High Court of Karnataka in the case of *CIT v. L.K. Trust, 297 ITR 53 (Kar)*.

55. The Id. counsel for the assessee made an alternative submission that if the interest expenditure disallowance is upheld, then the rate of interest that should be applied should be the average rate in respect of all the borrowings of the assessee because mixed funds were used for the purpose of giving advances or acquiring shares. No such plea was put forth by the assessee before the lower authorities and therefore at this stage it is not possible to entertain such a claim. Even before the Tribunal, no details have been furnished by the assessee in this regard. Therefore, the alternate plea of assessee is also rejected.

56. In the result, the appeal by the assessee is dismissed.

ITA No.387/Bang/2017

57. This appeal by the assessee is against the order dated 30.11.2016 of the CIT(Appeals)-3, Bengaluru relating to assessment year 2012-13.

58. 56. The only issue that arises for consideration in this appeal is with regard to disallowance of interest expenses u/s. 36(1)(iii) of the Act. The facts are identical to the facts as it prevailed in the AY 2011-12. For the year under consideration the Assessee has made the following advances to various group concerns.

- i. Rs.82,00,21,765 paid to Umbel Properties (P) Ltd. claimed to be for allotment of convertible/redeemable Debentures.
- ii. Rs.15,34,00,000/- advanced to Embassy Real Estate and Properties Holdings (P) Ltd., claimed to be for allotment of shares.
- iii. Rs.27,35,21,016/- advanced to Embassy Property Development (P) Ltd., for investment in business ventures.

- iv. Rs.20,81,56,253/- advanced to DM Estates (P) Ltd., and GV Properties (P) Ltd., as inter corporate deposits.

The total amount of the advances as stated above was Rs.145.50 crores. In addition to the above, the Assessee had also invested a sum of Rs.45 crores in shares of group company UPPL. The AO had taken into consideration the interest free advances made to various group concerns and was of the view that the interest bearing funds which were diverted to group concerns was not for the purpose of business. Accordingly, the AO made disallowance of interest amounting to Rs.31.26 crores on a proportionate basis taking into account the total interest expenditure incurred by the Assessee and the amount of interest free advances made to group concerns.

59. On appeal, the CIT(Appeals) confirmed the order of AO and held that the Assessee failed to prove that the above advances/investments were for the purpose of business of the Assessee. The CIT(A) held that the Assessee did not furnish any specific details to establish the existence of commercial expediency in respect of the amounts advanced to Embassy Property Development (P) Ltd and Embassy Real Estate and Properties Holding (P) Ltd. Similarly with regard to the inter corporate deposits advanced to GV Properties (P) Ltd., and DM Estates (P) Ltd., no specific information has been furnished with regard to the specific utilization of the money advanced to these companies to demonstrate the existence of business expediency. Therefore considering the specific facts of the case and in the absence of specific evidence with regard to the utilization of the money by the group companies, the CIT(A) held that the loans and advances in question cannot be said to be for the purpose of business.

60. The Assessee claimed before the CIT(A) the advances made to the group companies were not made out of interest bearing funds and own funds of the Assessee. The Assessee also furnished a working of interest which can be disallowed u/s 36(1) (iii). The CIT(A) found that the claim has not been demonstrated with specific facts and figures. He also found that the total amount of Share capital of the Assessee was only Rs.20 lakhs. The total reserves was negative i.e., (-) Rs.98.39 crores as on 31.03.2012 in view of the deficit in the Profit & Loss account. Therefore the CIT(A) rejected the contention of the Assessee that the advances to group companies were made out of the own funds of the company is contrary to the fact presented in the financial statements.

61. The Assessee also presented a statement showing the amount of interest which could be disallowed based on its own working. As per the statement the total amount of interest which could be disallowed u/s 36(1)(iii) is stated to be Rs. 785.73 lakhs. However the CIT(A) noticed that the Assessee had taken into consideration the non-interest bearing funds to the extent of Rs.382 crores comprising of long term liabilities, other current liabilities and depreciation written off. The CIT(A) held that it cannot be accepted that the long term and current liabilities have been utilized to finance the loans and advances paid to group companies. Hence, the CIT(A) held that the Assessee has not demonstrated how the advances to the group companies were made out of the current liabilities and depreciation written off. Therefore the contention of the appellant made in this regard was also not accepted by the CIT(A).

62. The Assessee claimed before the CIT(A) that the AO has taken into consideration Rs.1,61,63,11,120/- as the advance given to related concerns but the correct figure is Rs.145,50,99,834/-. The CIT(A) directed the AO to verify the amount and adopt the correct amount of advance for computing the disallowance.

63. The Assessee claimed before CIT(A) that it had received interest of Rs.3,61,86,594/- from the group companies in respect of the advances made. The Assessee furnished the financial statements to substantiate its claim in this regard. The CIT(A) held that interest of Rs.3,61,86,594/- was included under the head "Other income" as interest on loans and securities and interest on deposits, which was evident from Note 19 of the 'Note on Accounts'. The CIT(A) held that the amount of interest disallowance made by the AO should be reduced by the amount of interest received from these companies. The AO was directed to delete disallowance of interest to the extent interest income was received on advances and offered to tax.

64. Aggrieved by the order of the CIT(A), the Assessee has preferred the present appeal before the Tribunal.

65. Before the Tribunal, the Id. counsel for the assessee made a prayer that as per Schedule 18 and Schedule 8 to the P&L account and balance sheet, it had sufficient own funds and this needs to be looked into by the AO. We have considered the submission and we find that the CIT(Appeals) has elaborately discussed the availability of own funds, which has not been shown to be incorrect by the Id. AR before us. In these circumstances, we find no merit in this appeal and accordingly the same is dismissed.

ITA No.339/Bang/2017 and IT(TP)A No.384/Bang/2017

66. ITA No.339/B/17 is an appeal by the assessee, while IT(TP)A No.384/B/17 is an appeal by the revenue. Both these appeals are against the order of the CIT(Appeals)-3, Bengaluru dated 30.11.2016 relating to assessment year 2013-14.

67. As far as the appeal of revenue is concerned, the same is in relation to disallowance u/s. 14A of the Act. The CIT(Appeals) deleted the addition made u/s. 14A of the Act on the ground that the assessee did not earn any exempt income during the previous year and following several decisions wherein it was laid down that if there was no exempt income earned during the previous year, there can be no disallowance of expenses u/s. 14A of the Act. At the time of hearing of this appeal, it was brought to our notice by the Id. counsel for the assessee that the admitted factual position in the present case is that there was no dividend income or other exempt income earned by the assessee during the relevant previous year. The Id. counsel for the assessee drew our attention to the decision of the Bangalore Bench of ITAT in the case of M/s UB Infrastructure Projects Ltd., Vs. DCIT, ITA No. 2098/Bang/2016 (asst. year 2012-13) order dated 22/12/2017, wherein this Tribunal took the view that there can be no disallowance of expenses u/s 14A of the Act, if there is no exempt income earned during the relevant previous year. The following are the relevant observations of the Tribunal in this regard.

“3. Having carefully examined the orders of authorities below, we find that undisputedly the assessee has not earned any exempted income. Now it is settled position of law that whenever assessee did not earn any exempt income, no disallowance could be made u/s. 14A of the Act. The Hon’ble Delhi High Court in the case of Cheminvest Ltd. v. CIT, 378 ITR 33 (Del) has categorically held that section 14A envisages that there should be actual receipt of

income which was not includible in the total income during the relevant previous year for the purpose of disallowing any expenditure in relation to the said income. Wherever there is no exempt income includible in the total income of the assessee, the provisions of section 14A cannot be invoked. The relevant observations of the judgment of the Hon'ble Delhi High Court are extracted hereunder:-

“15. Turning to the central question that arises for consideration, the court finds that the complete answer is provided by the decision of this court in CIT v. Hololcim India (P) Ltd. (decision dated 5th September 2014, in I.T. A. No. 486 of 2014). In that case, a similar question arose, viz., whether the Income-tax Appellate Tribunal was justified in deleting the disallowance under section 14A of the Act when no dividend income had been earned by the assessee in the relevant assessment year ? The court referred to the decision of this court in Maxopp Investment Ltd. (supra) and to the decision of the Special Bench of the Income-tax Appellate Tribunal in this very case, i.e., Cheminvest Ltd. v. CIT [2009] 317 ITR (AT) 86 (Delhi) [SB]. The court also referred to three decisions of different High Courts which have decided the issue against Revenue. The first was the decision in CIT v. Lakhani Marketing Incl. (decision dated April 2, 2014, of the High Court of Punjab and Haryana in I. T. A. No. 970 of 2008)--since reported in [2015] 4 ITR-OL 246 (P&H)--which in turn referred to two earlier decisions of the same court in CIT v. Hero Cycles Ltd. [2010] 323 ITR 518 (P&H) and CIT v. Winsome Textile Industries Ltd. [2009] 319 ITR 204 (P&H). The second was of the Gujarat High Court in CIT v. Corrttech Energy (P.) Ltd. [2014] 223 Taxmann 130 (Guj) ; [2015] 372 1TR 97 (Guj) and the third of the Allahabad High Court in CIT v. Shivam Motors (P) Ltd. (decision dated 5th May, 2014, in T.A. No. 88 of ITA No.1 1071Bang12016 2014). These three decisions reiterated the position that when an assessee had not earned any taxable income in the relevant assessment year in question "corresponding expenditure could not be worked out for disallowance."

4. This was also examined by the Tribunal in the assessee's own case for assessment year 2010-11 and held that when there is no exempt income, provision of section 14 of the Act cannot be applied.

5. In the light of the aforesaid judgment, the provisions of section 14A cannot be invoked as there is no exempt income in the hands of the assessee. Accordingly, we find no infirmity in the order of the CIT(Appeals) who has rightly deleted the addition.”

68. In view of the aforesaid decision of the Tribunal, we are of the view that the disallowance of expenditure u/s 14A of the Act was rightly deleted by the CIT(A).

69. As far as the appeal by the assessee is concerned, the only issue that arises for consideration in this appeal is with regard to disallowance of interest u/s. 36(1)(iii) of the Act. The facts and circumstances under which disallowance of interest was made by the revenue authorities and the submissions of the Assessee are identical to the facts and submissions of the Assessee, as it prevailed in the AY 2012-13. For reasons given while deciding similar issue in AY 2012-13, we find no merit in this appeal by the assessee. Accordingly, the same is dismissed.

70. In the result, the appeal of the revenue in ITA No.384/Bang/2017 is dismissed.

71. In the combined result, the following appeals by the Assessee viz., ITA No.333/Bang/2017 (For AY 2007-08) is dismissed, ITA Nos.334, 335 & 336/Bang/2017 (For AY 2008-09 to 2010-11) are partly allowed for statistical purposes, ITA Nos.337, 338 & 339/Bang/2017(For AY 2011-12 to

2013-14) and the following appeal by the Revenue, viz., ITA No.384/Bang/17 (for AY 2013-14) is dismissed.

72. Pronounced in the open court on this 10th day of May, 2019.

Sd/-

(JASON P. BOAZ)
ACCOUNTANT MEMBER

Sd/-

(N.V. VASUDEVAN)
VICE PRESIDENT

Bangalore,
Dated, the 10th May, 2019.

/ Desai Smurthy /

Copy to:

1. The Appellant
2. The Respondent(s)
3. The CIT
4. The CIT(A)
5. The DR, ITAT, Bangalore.
6. Guard file

By order

Assistant Registrar,
ITAT, Bangalore.