

IN THE INCOME-TAX APPELLATE TRIBUNAL "E" BENCH MUMBAI
BEFORE SHRI PAWAN SINGH, JUDICIAL MEMBER AND
SHRI RAMIT KOCHAR, ACCOUNTANT MEMBER
ITA No. 709/Mum/2018 (Assessment Year 2014-15)

ACIT, Circle-2(3)(1), R.No. 552, 5 th Floor, Aayakar Bhavan, M.K. Road, Mumbai-400020.	Vs.	M/s Trust Capital Services (India) Pvt. Ltd., 105, Vikas, 11 Bank Street, Fort, Mumbai-400023. PAN: AABCT3654P
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Appellant

Respondent

Appellant by : Shri V.K. Chaturvedi (Sr.DR)

Respondent by : Shri Sanjay Parikh (AR)

Date of Hearing : 10.04.2019

Date of Pronouncement : 31.05.2019

ORDER UNDER SECTION 254(1) OF INCOME TAX ACT

PER PAWAN SINGH, JUDICIAL MEMBER;

1. This appeal by revenue under section 253 of Income-tax Act ('Act') is directed against the order of Id. Commissioner of Income-tax (Appeals)-6, Mumbai [hereinafter referred as Id. CIT(A)] dated 15.11.2017 for Assessment Year 2014-15, which in turn arises from the assessment order dated 29.12.2016 passed under section 143(3) of the Act. The revenue has raised the following grounds of appeal:

1. "On the facts and in the circumstances of the case and in law, the Ld. CIT (A) has erred in partially deleting the disallowance made u/s 36(1)(iii) of the Act without appreciating the fact that the assessee being a Non-Banking Financial Company paid higher rate of interest to its lenders than the rate of interest received on loans extended by it."

2. On the facts and in the circumstances of the case and in law, the Ld.CIT(A) has erred in deleting the notional loss debited by the assessee in

the P&L account without considering the fact that the provision for loss made by the assessee was contingent in nature and the same should have been disallowed as per CBDT instruction no.3/2010 dated 23.03.2010".

3. On the facts and in the circumstances of the case in law, the Ld. CIT(A) has erred in deleting disallowance u/s. 14A of the Act without appreciating the fact that Revenue has filed further appeal on the same issue before Hon'ble Supreme Court in the case of Cheminvest Ltd."

2. Brief facts of the case are that the assessee is a company engaged in the business of investment in securities. The assessee filed its return of income for Assessment Year 2014-15 on 30.11.2014 declaring total income of Rs. 10,40,99,210/-. The return of income was selected for scrutiny and the assessment was completed on 29.12.2016 under section 143(3) of the Act. The Assessing Officer while passing the assessment order made the addition of Rs.62,71,660/- under section 36(1)(iii), addition of Rs.64.24,201/- on account of market to market loss and disallowance of Rs. 15,88,675/- under section 14A. On appeal before the Id. CIT(A), the assessee was allowed partial relief on the addition under section 36(1)(iii), however, remaining other additions/disallowance was deleted. Thus, aggrieved by the order of Id. CIT(A), the revenue has filed the present appeal before us.
3. We have heard the submissions of the Id. DR for the revenue and the Id AR for the assessee and perused the material available on record. We have also deliberated on various case laws relied by the lower authorities and the Id. representatives of the parties. Ground No.1 relates to sustain

the partial the disallowance of interest expenses under section 36(1)(iii). The Id. Departmental Representative (DR) for the revenue supported the order of Assessing Officer. The Id. DR submits that the assessee during the relevant period the assessee has availed loan from M/s Infoline Finance and paid interest @ 16%. However, the assessee has charged lesser interest @ 12% per annum for loans given to the same company. Besides that the assessee has also charged interest from the related parties at a lower rate of interest average rate of interest of 8.968% whereas the assessee has paid charges at average rate interest of 10.97%. The assessee also charged interest from related party @ 8% and paid interest to Sankhya Financial Services P. Ltd. @ 14%. The Assessing Officer worked out the addition/disallowance by taking average rate of interest (-) average rate of interest received and multiplied with total amount of interest received (-) interest received from M/s India Infoline Finance Ltd. (supra) and divided by average rate of interest received and worked out excess interest of Rs. 62.71 lakhs. The AO was of the view that the assessee had failed to explain commercial expediency in granting loans at lower rate of interest. The Id. CIT(A) deleted the interest of Rs. 4,65,753/- against the interest payment to M/s India Infoline Finance Ltd. as in the opinion of the learned CIT(A) the said party India Infoline Finance Limited is an NBFC where in commercial realty NBFC's have higher lending rates and lower deposits . Further it was observed by

learned CIT(A) that the said India Infoline Finance Limited is not a related party. The learned CIT(A) deleted the said addition by holding that interest paid by assessee to India Infoline Finance Limited was for business purposes and ordered for deletion of disallowance of Rs. 4,65,753/- as was made by AO u/s 36(1)(iii) of the 1961 Act. With respect to disallowance of interest paid to related parties wherein the AO had alleged that borrowing costs were higher than lending rates to these related parties while disallowing interest expenses, the learned CIT(A) observed that factually the interest paid to one related party is higher, while interest receivable from all of them is at 8% only. The learned CIT(A) was of the view that it is for the assessee to demonstrate while dealing with related parties as to commercial expediency in borrowing at higher rate of interest while lending at lower rate of interest. The learned CIT(A) affirmed the action of AO in disallowance of differential interest rates u/s 36(1)(iii) of the 1961 Act . The learned CIT(A) also applied provisions of Section 40A(2)(b) of the 1961 Act. The learned CIT(A) after analyzing the details also observed that assessee has also borrowed from related parties @8% and thus the learned CIT(A) ordered the disallowance to be recomputed by restricting the same towards differential interest rate of 6% in case of Sankhya Financial Services P. Ltd.. The ld. DR for the revenue prayed for reversing the order of ld CIT(A) and restoring the order of Assessing Officer.

4. On the other hand, the ld. AR of the assessee supported the order of Id. CIT(A). The ld. AR of the assessee submits that assessee had given advance to M/s India Infoline Finance Ltd. and charged interest @ 12%. The assessee also received a loan from M/s India Infoline Finance Ltd. and paid interest @ 16%. The assessee received interest of Rs. 24.57 lakhs and paid interest of Rs. 18.63 lakhs to said party India Infoline Finance Limited. The Assessing Officer accordingly disallowed excess interest @ 4% of Rs. 4,64,753/-, which decision of AO was reversed by learned CIT(A) as the said party is NBFC and not a related party . The decision of the assessee to pay this differential interest were held to be governed by commercial expediency. The ld. AR of the assessee further submits that the assessee had borrowed fund at a short notice and for a short period of time i.e. at the time of settlement. Immediately after payment is made for settlement and money is recovered from the client, the loan was re-paid that is why the assessee paid interest at higher rate i.e @ 16% which was a short term loan. The assessee gave loan to M/s India Infoline Finance Ltd. as Inter Corporate Deposit (ICD) for a longer period. Accordingly, the interest rate of such ICD given was at a lower rate of interest. M/s India Infoline Finance Ltd. is not a related entity with the assessee. Further, being corporate entity, the tax rate applicable to M/s India Infoline Finance Ltd. and assessee are same. The difference in interest paid was only on account of immediate demand, supply need

and business expediency. For disallowance in respect of remaining other parties of Rs. 58,05,907/-, the Id. AR of the assessee submits that assessee has taken short term borrowings in order to meet its commitment at the time of settlement. Therefore, the assessee is required to borrow the funds from whatever sources available at whatever competitive rate of interest the loan is available in market. Most of the parties who provided loan are corporate assessee. The interest paid to unrelated party are 13% to 14% & 8% to related party. The assessee charged interest @ 12% from unrelated parties and @ 8% from related parties. In most of the cases, the assessee has generally paid and received interest @ 8% from related parties, except Sankhya Financial Services P. Ltd., which is a Non-Banking Financial Company (NBFC) which given loan to the assessee out of borrowings for which, the assessee had to pay interest @ 14%. The Id. CIT(A) after appreciating the fact rightly deleted the addition/disallowance of Rs. 4,65,753/- out of interest paid to M/s India Infoline Finance Ltd. Similarly for Sankhya Financial Services P. Ltd., which is related party the differential rate of interest i.e 6% as borrowing rates were 14% while lending rate was 8% was disallowed by learned CIT(A), which disallowance is accepted by assessee and no challenge is made to such disallowance upheld by learned CIT(A).

5. We have considered the submission of both the parties and gone through the order of authorities below. We have also deliberated on various case

laws relied by lower authorities and Id. Representative of the parties. During the assessment proceedings, the Assessing Officer noted that assessee has paid interest at a higher rate of loans taken from M/s India Infoline Finance Ltd., however, assessee has charged interest at lower rate for loans given to the same company. The assessee paid interest @ 16% per annum, however, charged interest @ 12% from the same company. The assessee also charged the interest from the related party at the lower interest average @ 8.96% whereas; the assessee has paid interest at average rate of 10.97%. Similarly, the assessee has paid interest @ 14% to Sankhya Financial Services P. Ltd. The Assessing Officer identified all those parties to which assessee either charged interest or paid interest during the relevant Financial Year. The Assessing Officer worked out the disallowance/addition in the following manner:

India Infoline Finance Ltd. interest disallowance

$$18,63,014 \times 16 - 12 \text{ (differential interest rate) } / 16 = 4,65,753$$

Interest disallowance of other parties

(Avg. rate of interest paid- Avg. rate of interest received) X (total amount of interest received-interest received from India Infoline)/ avg. rate of interest received

$$(10.971\% - 8.9618\%) \times (28356678 - 2457534) / 8.9618 =$$

$$2.009 \times 25899144 / 8.9618 = 58,05,907$$

6. The Id. CIT(A) while considering the submission of assessee divided the transaction in two parts i.e. (i) with M/s India Infoline Finance Ltd. and (ii) other related entities. For the transaction with M/s India Infoline

Finance Ltd., the Id. CIT(A) observed that the assessee has taken short term borrowing to meet the settlement needs of interest futures. The M/s India Infoline Finance Ltd. is a NBFC which is deals in taking deposit and lending the money. The Id. CIT(A) further observed that in commercial reality, the loan rates of Bank of NBFC were higher than interest paid on deposit. M/s India Infoline Finance Ltd. is not a related party, thus it cannot be said that interest paid to them is not for business purpose. Therefore, the disallowance was treated as unjustifiable and deleted the same accordingly.

7. So far as disallowance of interest to related parties are concerned, the Id. CIT(A) observed that the interest paid to only related party is higher, whereas the interest received from all of them is at 8% only. The Id. CIT(A) further observed that the assessee has to demonstrate the business expediency and need while dealing with related parties for payment of interest at higher rate and or charging less rate of interest. As simple and self serving statement is not sufficient. The Id CIT(A) observed that the Assessing Officer has prepared a complete chart of interest rate chart and paid in a tabular format in para 6.1 of his order. The Id. CIT(A) further observed that party no. 1 to 8 are related parties and the interest paid and received from those parties are @ 8% except in case of Sankhya Financial Services P. Ltd. Thus, the disallowance consequential to difference interest rate has rightly been done by

Assessing Officer as provision of section 40A(2)(b) would also be applicable. The Id. CIT(A) further observed that there are instances that interest paid to related parties at 8% and therefore, the disallowance made by Assessing Officer would be justified to be restricted to only one case on Sankhya Financial Services P. Ltd. whereas the difference rate of interest is at 6%. Therefore, the Assessing Officer was directed to re-compute the disallowance of interest by taking justifiable rate to Sankhya Financial Services P. Ltd. @ 8% only and granted partial relief to the assessee. The assessee has not challenged the disallowance as were affirmed by learned CIT(A) with respect of interest rate differential Sankhya Financial Services Private Limited.

8. We have noted that the Id. CIT(A) passed the order after properly appreciating the fact and directed to recompute the interest disallowance. We have observed that the said party M/s India Infoline Finance Limited is an unrelated party. It is explained by the assessee before the authorities below that the assessee is in the business of trading in interest futures and borrowing are made at shorter notice for a shorter period to meet immediate fund requirements at the time of settlement and once money is recovered from clients, the loans and advances are repaid. It was explained that the loan borrowed from India Infoline Finance Limited @16% was a short term loan while loan granted to India Infoline Finance Limited was an Inter Corporate Deposit for a longer period and

hence lower rate of interest @12% was charged. This is a plausible view offered by the assessee governed by principles of commercial expediency and the onus which lay on assessee stood discharged . Now it was for Revenue to have rebutted the same with cogent evidences that the said decision was not governed by principles of commercial expediency . Merely because while dealing with a party who is an NBFC, the borrowing rates are higher than lending rate , inferences cannot be drawn against the tax-payer in a straight jacket manner. The terms and conditions of borrowing/lending in totality as well surrounding circumstances governing such business decision ought to have been evaluated by AO to rebut the contentions of the assessee. The AO failed to do so and further the AO cannot sit in the arm chair of businessmen and decide about commercial expediency of business decision taken by tax-payer. With respect to other disallowance of interest rate differential made by the AO which were deleted by learned CIT(A) , we have observed from the chart of borrowings and lending as reproduced by learned CIT(A) in para 6.1 that the assessee has borrowed from related parties at 8% and loans were also granted to related parties at 8% . The major borrowings were from Trust Investment Advisor Private Limited , a related party wherein interest @ 8% was payable amounting to Rs. 3.00 crores. So far as allegation of lending at lower rate of interest to JM Financial Services Limited @0.5% is concerned , it is explained by

assessee that the assessee has paid Rs. 22.69 lacs to JM Financial Services Private Limited towards processing charges / brokerage for arranging loan from M/s JM Financial Products Limited . If the processing charges/brokerage for arranging loans are paid, we fail to understand how the same can be considered for computing disallowance based on interest rate differential. So far as disallowance confirmed by learned CIT(A) with respect to interest rate differential to a related party namely Sankhya Financial Services Private Limited , the assessee has accepted the same and no appeal/CO is filed by the assessee. The chargeability of interest on loans granted by a taxpayer vis-a-vis interest payable on borrowings are commercial decisions taken by a tax-payer based on commercial expediency. There are several factors which govern these decisions such as period of loan, terms of loan, immediate pressing business needs , securities offered etc for borrowing/lending. The Revenue cannot sit in the arm chair of businessmen and start scrutinizing these decisions without analyzing the several complex reasons which govern decision making process undertaken by a businessman unless it is shown that malafide is writ large with a view to defraud Revenue. In our view the ld CIT(A) has take a reasonable view, which we affirm. No contrary fact or law is brought to our notice to take any other view. Therefore, we do not find any justification to interfere with the finding of ld. CIT(A). In the result, ground no.1 of the appeal is dismissed.

9. Ground no.2 relates to disallowance of market to market loss. The ld. DR for the revenue supported the order of Assessing Officer. The ld. DR further submits that Assessing Officer while going through the Profit & Loss Account noted that assessee has incurred notional loss of Rs. 64,24,201/-. The loss being notional in nature which is only contingent and was disallowed as per provision of section 37.
10. On the other hand, the ld. AR of the assessee submits that this ground of appeal is covered by the decision of Hon'ble Bombay High Court and the decision of Tribunal in support of his submission, the ld. AR of the assessee relied upon the decision of Hon'ble Bombay High Court in DIT(IT) vs. Citybank [377 ITR 69], CIT vs. D. Chatan & Company [390 ITR 36 (Bom)], DCIT vs. Bank of Bahrain and Kuwait [2010] 5 ITR (Trib.) 301 (Mum) (SB), IDBI vs. Capital market Services Ltd. vs. DCIT [2015] 42 ITR (Trib.) 379 (Mum).
11. We have considered the rival submission of the parties and have gone through the orders of lower authorities. We have observed that the assessee is trading in interest rate futures. The assessee has claimed losses as on year end based on open positions of interest rate futures. These interest rate futures are traded in stock exchanges. The copies of contract notes are placed in paper book. The assessee has claimed the same to have accrued due to fluctuation in market rates prevailing on stock exchange as at year end. The assessee has claimed that it followed

generally accepted accounting principles and it is not a contingent or notional loss as the said loss crystallized due to adverse rate movements in interest rate futures as at year end. We have also deliberated on various case law referred and relied by lower authorities and by Id. Representative of the parties. The Assessing Officer disallowed the marked to market loss considering the same to be notional in nature and for the reasons that appellant has not submitted any actual gain or loss in the next year. We have noted that Id. CIT(A) granted relief to the assessee by following the decision of Tribunal in IDBI vs. Capital market Services Ltd.(supra) and the decision of Special Bench in DCIT vs. Bank of Bahrain and Kuwait (supra). The Id. CIT(A) further concluded that the assessee has made submission to Assessing Officer regarding financial outcome of derivative in the next year during the assessment, copy of which was also furnished for the perusal of Id. CIT(A), therefore, the Id. CIT(A) by following the decision of IDBI vs. Capital market Services Ltd.(supra) directed the Assessing Officer to delete the disallowances. In our considered view also this loss is not a notional loss or contingent loss as infact the loss crystallized as at year end due to adverse price movements of derivatives in stock market. No contrary law or fact is brought to our notice to deviate from the finding of Id. CIT(A). In the result, ground no.2 of the appeal is also dismissed.

12. Ground no.3 relates to disallowance under section 14A. The ld. DR for the revenue supported the order of ld. Assessing Officer.
13. On the other hand, the ld. AR of the assessee submits that during the relevant Financial Year, the assessee has not earned any exempt income; therefore, no disallowance under section 14A is warranted. In support of his submission, the ld. AR of the assessee relied upon the decision of jurisdictional High Court in PCIT vs. Balarpur Industries Ltd. (ITA No. 51/2015 dated 13.10.2016).
14. We have considered the submission of both the parties and have perused the order of lower authorities. We have also deliberated on various case law relied by respective parties. The Assessing Officer noted that the assessee has made investment of Rs. 7.36 Crore out of total non-current investment of Rs. 39.16 Crore in unlisted equities and mutual fund. The Assessing Officer while relying upon the decision of Special Bench in Mumbai Tribunal in M/s Daga Capital Management Pvt. Ltd. invoked the provision of section 14A r.w.r. 8D and worked out the disallowance of Rs. 15,88,675/-. Before the ld. CIT(A), the assessee contended that the assessee has not earned any dividend income during the relevant financial year, therefore, there was no question of disallowance under section 14A. The ld. CIT(A) deleted the entire disallowance by following the decision of Hon'ble Delhi High Court in Cheminvest Ltd. vs. CIT 9378 ITR 33).

15. We have further noted that the jurisdictional High Court PCIT vs. Balarpur Industries Ltd. (supra) by following the decision of Hon'ble Delhi High Court in ITA No. 749/2014 held that the provision of section 14A would not apply, if no exempt income was received or receivable during the relevant previous year. Considering the above factual and legal discussion we do not find any illegality or infirmity in the order passed by Id. CIT(A), which we affirm. In the result the ground No.3 of the appeal is also dismissed.

16. In the result, appeal of the revenue is dismissed.

Order pronounced in the open court on 31/05/2019.

Sd/-
RAMIT KOCHAR
ACCOUNTANT MEMBER

Mumbai, Date: 31.05.2019
SK

Copy of the Order forwarded to :

1. Assessee
2. Respondent
3. The concerned CIT(A)
4. The concerned CIT
5. DR "E" Bench, ITAT, Mumbai
6. Guard File

Sd/-
PAWAN SINGH
JUDICIAL MEMBER

BY ORDER,

Dy./Asst. Registrar
ITAT, Mumbai