

**IN THE INCOME TAX APPELLATE TRIBUNAL  
(DELHI BENCH 'I-1' : NEW DELHI)**

**BEFORE SHRI R.K. PANDA, ACCOUNTANT MEMBER  
and  
SHRI KULDIP SINGH, JUDICIAL MEMBER**

**ITA No.1384/Del./2017  
(Assessment Year : 2013-14)**

M/s. Jaypee Capital Services Ltd., vs. DCIT, Central Circle 29,  
FA – 45, Lower Ground Floor, New Delhi.  
Shivaji Enclave,  
New Delhi.

**(PAN : AAACJ0628A)**

**(APPELLANT)**

**(RESPONDENT)**

ASSESSEE BY : Shri Ved Jain, CA  
Shri Ashish Goel, CA  
Shri Akshit Goel, CA

REVENUE BY : Shri B. Ramanjaneyulu, Senior DR

Date of Hearing : 06.01.2020

Date of Order : 17.01.2020

**ORDER**

**PER KULDIP SINGH, JUDICIAL MEMBER :**

Appellant, M/s. Jaypee Capital Services Ltd. (hereinafter referred to as 'the assessee') by filing the present appeal sought to set aside the impugned order dated 30.01.2017 passed by Commissioner of Income-tax (Appeals) – 30, New Delhi qua the Assessment Year 2013-14 on the grounds inter alia that:-

*“On the facts and circumstances of the case, the order passed by the learned Commissioner of Income Tax (Appeals) [CIT(A)] is bad both in the eye of law and on facts.*

2. (i) *On the facts and circumstances of the case, the learned CIT(A) has erred, both on facts and in law, in confirming the disallowance of an amount of Rs.55,73,9701- made by the AO invoking the provisions of Section 14A read with Rule 8D.*

(ii) *That the learned the CIT(A) has erred in confirming the disallowance rejecting the contention of the assessee that no expenditure on earning tax free income has been incurred by the assessee.*

3. *On the facts and circumstances of the case, the learned CIT(A) has erred both on facts and in law in rejecting the contention of the assessee that the shares having been held by the assessee as stock-in-trade for regular business of the assessee, the dividend income on such shares being incidental, the disallowance under Section 14A is not called for.*

5. *Without prejudice to the above and in the alternative, the learned CIT(A) has erred in rejecting the contention of the assessee that the investments being strategic in nature the dividend is only incidental, therefore disallowance under Section 14A is not called for.*

5. *Without prejudice to the above and in the alternative, the assessee having sufficient owned funds, investments having not been made out of borrowed funds, no disallowance of interest under Section 14A can be made.*

6. (i) *On the facts and circumstances of the case, the learned CIT(A) has erred both on facts and in law in confirming disallowance of an amount of Rs.24,15,000/- made by the AO on account of interest under Section 36(1)(iii) of the Act.*

(ii) *That the disallowance has been confirmed rejecting the contention of the assessee that the impugned advances have been made out of business expediency.*

7. *Without prejudice to the above and in the alternative, the assessee having sufficient owned funds, the loans having not been given out of borrowed funds, disallowance under Section 36(1)(iii) is not called for.*

8. *Without prejudice to the above and in the alternative, the calculation of disallowance of interest under Section 36(1)(iii) made by the AO is wrong.*

9. (i) *On the facts and circumstances of the case, the learned CIT(A) has erred both on facts and in law in confirming disallowance of an amount of Rs.4,48,911/- made by the AO on account of foreign tours and travel expenses.*

(ii) *That the disallowance has been confirmed despite the expenses being incurred wholly and exclusively for the purposes of business.*

(iii) *That the disallowance has been confirmed rejecting the contention of the assessee that Shri Saurav Arora, Director of the company having gone on foreign tour for business purposes, the disallowance is not called for.*

10. (i) *On the facts and circumstances of the case, the learned CIT(A) has erred both on facts and in law in confirming addition of an amount of Rs.1,41,95,888/- on account of difference in arm's length price on interest on equity provided to the foreign subsidiary.*

(ii) *On the facts and circumstances of the case, the learned CIT(A) has erred both on facts and in law in rejecting the contention of the assessee that the action of the AO in making the above said addition under Section 92 of the Act without referring the case to the Transfer Pricing Officer is bad in law.*

(iii) *On the facts and circumstances of the case, the learned CIT(A) has erred both on facts and in law in rejecting the contention of the assessee that the act of the AO in making the above said addition without bringing any comparable on record to determine the arm's length price is bad in law.*

11. (i) *On the facts and circumstances of the case, the learned CIT(A) has erred both on facts and in law in rejecting the contention of the assessee that the transaction of providing equity to the AE is not an international transaction as defined under Section 92B of the Act.*

(ii) *That the transaction of providing equity does not have any impact on profits or assets of the assessee, the same is not an international transaction.*

(iii) *On the facts and circumstances of the case, the learned CIT(A) has erred both on facts and in law in rejecting the contention of the assessee that the AO has erred in re-characterizing the transaction of providing equity into a loan transaction.*

12. *On the facts and circumstances of the case, the learned CIT(A) has erred both on facts and in law in confirming the*

*action of the AO in treating the amount of Rs.10,51,54,723/- standing in the name of the assessee in the last year as a loan given to the subsidiary during the current year also.*

*13. Without prejudice to the above and in the alternative, the learned CIT(A) has erred in rejecting the contention of the assessee that the transaction being in foreign currency the LIBOR rate is the appropriate rate of interest, not the rate as applied by the AO."*

2. Briefly stated the facts necessary for adjudication of the controversy at hand are : M/s. Jaypee Capital Services Ltd., the assessee company is into the business of trading of equity, commodity and derivatives of equity and forex market. Assessee company is also into trading of shares through recognized stock exchanges viz. National Stock Exchange (NSE), Bombay Stock Exchange (BSE), etc. Initially, assessee company had filed return of income on 30.09.2013 declaring total income at Rs.1,89,260/-, which was subsequently revised by declaring income of Rs.22,42,240/- declaring interest income of Rs.21,83,329/- on FDRs.

3. From the financials of the assessee company, Assessing Officer (AO) noticed that the assessee company paid interest expenses to the tune of Rs.81,33,342/- on the funds borrowed. Declining the contentions raised by the assessee that interest expenses claimed in profit & loss account of interest which was paid on the loan was required for running the business activities.

AO made addition of Rs.24,15,000/- under section 36 (1)(iii) of the Income-tax Act, 1961 (for short 'the Act'). AO by invoking the provisions contained u/s 14A of the Act read with Rule 8D of the Income-tax Rules, 1962 (for short 'the Rules') made disallowance of Rs.55,73,970/-. AO also made disallowance of Rs.4,48,911/- on account of foreign tours and travel expenses on the ground that Shri Saurav Arora is neither Director nor employee of the assessee company nor the assessee company has conducted any transaction in Australia and New Zealand stock exchanges.

4. AO also made an addition of Rs.1,41,95,888/- on account of difference in the arm's length price on interest on equity provided to the foreign subsidiary. AO also treated the amount of Rs.10,51,54,723/- standing in the name of the assessee in the last year as a loan given to the subsidiary during the current year and thereby assessed the total income of the assessee at Rs.2,48,76,010/-.

5. Assessee carried the matter by way of appeal before the Id. CIT (A) who has confirmed the additions by dismissing the appeal. Feeling aggrieved, the assessee has come up before the Tribunal by way of filing the present appeal.

6. We have heard the Id. Authorized Representatives of the parties to the appeal, gone through the documents relied upon and

orders passed by the revenue authorities below in the light of the facts and circumstances of the case.

**GROUND NO.1**

7. Ground No.1 is general in nature, hence needs no adjudication.

**GROUNDS NO.2, 3 & 4**

8. Grounds No.2, 3 & 4 are dismissed having not been pressed during the course of arguments.

**GROUNDS NO.5, 6, 7 & 8**

9. Undisputedly, during the year under assessment, assessee company has earned dividend income of Rs.1,36,19,200/- and claimed the same as exempt u/s 10(34) of the Act. Ld. AR for the assessee challenging the impugned order contended that the entire investment in the shares have been made by the assessee company out of its own funds and drew our attention towards balance sheet, available at page 16 of the paper book. Perusal of the balance sheet qua the year under assessment shows that the assessee company is having paid up share capital of Rs.7,64,75,500/- with reserve and surplus of Rs.3,17,17,14,177/- (total Rs.3,24,81,89,677/-). These facts go to prove that as against the total investment of Rs.2,97,33,89,709/-, assessee company was having its own share capital and surplus & reserves to the tune of

Rs.3,24,81,89,677/- . It is settled principle of law that in case the assessee company is having sufficient own interest free funds, it is to be presumed that the investment is not made out of borrowed funds but out of its own interest free funds. Reliance in this regard is placed on the decision rendered by Hon'ble Supreme Court in case of *CIT vs. Reliance Industries Ltd. in Civil Appeal No.10 of 2019 dated 02.01.2019* and decision rendered by Hon'ble High Court of Punjab & Haryana in *CIT vs. Max India Ltd. in ITA No.186 of 2013 dated 06.09.2016*.

10. More-so, before invoking the provisions contained u/s 14A of the Act, AO has not recorded his satisfaction as required u/s 14A(2) that the working given by the assessee is not correct. Hon'ble High Court of Delhi in case of *Maxopp Investment Ltd. vs. CIT 347 ITR 272 (Del.)*, confirmed by Hon'ble Supreme Court, held that, "*it is incumbent upon the AO to record satisfaction as to the working given by the assessee that no expenses have been incurred by it to earn the dividend income*". In view of the matter, we are of the considered view that addition made by the AO and confirmed by the Id. CIT (A) u/s 14A is not sustainable, hence ordered to be deleted.

11. So far as addition of Rs.24,15,000/- made by the AO and confirmed by the Id. CIT (A) u/s 36(1)(iii) is concerned on account

of disallowance of interest is concerned, assessee company has come up with specific plea that it has not granted any loans to Futurz Next Services Pvt. Ltd. rather all are regular business transactions supported with regular receipt and payment transactions occurring in the account. It is also contended by the ld. AR for the assessee that all the transactions are attributed to the business of shares/future/option of securities and drew our attention towards its financial ledger for the period 01.04.2012 to 31.03.2013, available at pages 64 to 68 of the paper book wherein business transactions with Futurz Next Services Pvt. Ltd. have been recorded.

12. It is also contended by the ld. AR for the assessee that advances to the group companies have been given out of its own paid up share capital and reserve & surplus of Rs.3,24,81,89,677/- for commercial expediency to the group companies and relied upon the decision of *S.A. Builders Ltd. vs. CIT (2007) 158 taxman 74 (SC)*. So, in view of the financials brought on record by the assessee company discussed in the preceding para, we are of the considered view that since transactions are pertaining of business of shares/future/option of securities & advances having been given on account of commercial expediency of the group companies, disallowance made by the AO and confirmed by the ld.

CIT (A) u/s 36(1)(iii) is not sustainable, hence ordered to be deleted. So, grounds no.5, 6, 7 & 8 are determined in favour of the assessee.

**GROUND NO.9**

13. AO made disallowance of Rs.4,48,911/- on account of foreign tour and travel expenses incurred by Shri Saurav Arora which are pertaining to his travel to Australia and New Zealand on the ground that Shri Saurav Arora is neither Director nor employee of the assessee company and assessee company has not conducted any transactions with Australia and New Zealand Stock Exchanges and Id. CIT (A) also confirmed the disallowance.

14. Challenging the impugned order, Id. AR for the assessee contended that disallowance has been made and confirmed by AO/ CIT (A) by recording incorrect facts and drew our attention towards page 16 of the paper book which is balance sheet of the assessee company showing that Shri Saurav Arora is one of the Directors of the assessee company.

15. However, from the perusal of the reply filed by the assessee company before the Id. CIT (A), extracted in para 7.2 of the impugned order, assessee company has failed to prove the purpose for which foreign tours have been carried out by Shri Saurav Arora. Emails brought on record by the assessee company also

failed to explain the purpose of foreign visits. Perusal of the foreign detail given by the assessee company, available at page 50 of the paper book, also does not disclose the purpose and result of the foreign visits.

16. However, we are of the considered view that expenses of Rs.4,48,911/- incurred by Shri Saurav Arora, Director of the assessee company when not proved to be incurred for business purpose of the assessee company, its addition cannot be made against assessee company rather its addition can be made against Shri Saurav Arora in his individual capacity. In these circumstances, addition of Rs.4,48,911/- made in the name of assessee company is not sustainable, hence ordered to be deleted. So, ground no.9 is determined in favour of the assessee company.

**GROUND NO.10, 11, 12 & 13**

17. AO noticed investment made by the assessee company in foreign companies, namely, Jaypee Capital Inc., USA and Jaypee Singapore Pte Ltd.. AO made addition of Rs.1,04,24,675/- on account of arm's length price value of the interest receivable on loans outstanding in the name of Jaypee Singapore Pte Ltd. against which the assessee has shown nil interest. It is categoric plea of the assessee company that remittance to foreign subsidiaries has been made vide "capital infusion" in order to extend its business

and to keep its control over foreign subsidiaries. However, the AO has treated the “capital infusion” as deemed loan and thereby made addition on account of interest @ 13.5% on deemed loan as its arm’s length price value.

18. Assessee company has raised categoric plea that foreign subsidiaries in which capital infusion was made, is part of Jaypee Capital Services Pvt. Ltd. and as such, there is no question of charging interest on the same. It is contended by the ld. AR for the assessee that transaction of investment into loan cannot be recharacterized by the AO.

19. Undisputedly, for the year under assessment, there is no loan outstanding against the subsidiary. When we examine Notes on Financial Statement ending 31.03.2013, available at page 21 of the paper book, it is proved that investment has been made in equity shares of subsidiary of the assessee, namely, Jaypee Singapore Pte. Ltd. by way of infusion of capital in accordance with the RBI Guidelines under automatic approval route. Moreover, Jaypee Singapore Pte. Ltd. has made final allotment to the assessee company in AY 2014-15.

20. Hon’ble High Court of Delhi in case of *CIT vs. EKL Appliances Ltd.* 345 ITR 241 held as under :-

*“17. The significance of the aforesaid guidelines lies in the fact that they recognise that barring exceptional cases, the tax administration should not disregard the actual transaction or substitute other transactions for them and the examination of a controlled transaction should ordinarily be based on the transaction as it has been actually undertaken and structured by the associated enterprises. It is of further significance that the guidelines discourage re-structuring of legitimate business transactions. The reason for characterisation of such re-structuring as an arbitrary exercise, as given in the guidelines, is that it has the potential to create double taxation if the other tax administration does not share the same view as to how the transaction should be structured.*

*18. Two exceptions have been allowed to the aforesaid principle and they are (i) where the economic substance of a transaction differs from its form and (ii) where the form and substance of the transaction are the same but arrangements made in relation to the transaction, viewed in their totality, differ from those which would have been adopted by independent enterprises behaving in a commercially rational manner.”*

21. Similarly, coordinate Bench of the Tribunal in case of *Topsgrup Electronic System Ltd. vs. ITO (2016) 48 ITR (trib) 753* also held that re-characterization of capital transaction into loan by the Transfer Pricing Officer is not sustainable in the eyes of law in view of the decision rendered by Hon’ble Bombay High Court in case of *Besix Kier Dabhol SA 2012 (10) TMI 817 (Bombay)*. Operative part of the order is extracted for ready perusal as under:-

*“In this case the question before the court was: -*

*“i) Whether on the facts and circumstances of the case and in law the Tribunal was right in holding that in the absence of any specific thin capitalization rules in India, the Assessing Officer cannot disallow the interest payment on debt capital after having observed the abnormal thin capitalization ratio of 248:1?”*

*In this regard it was submitted that the Hon'ble Court held as under at paras 4 to 8 of its order: -*

"4) *The respondent-assessee is a company incorporated under the laws of Belgium. The sole business of the respondent-assessee is to carry out the project of construction of fuel jetty near Dabhol in India. The respondent-assessee had fully paid capital of 25.00 lacs (Belgium Francs) divided into 2500 shares of 1000 Belgium Francs each. This equity capital was divided in the ratio of 60:40 between the two joint venture partners N V Besix SA, Belgium and Kier International (Investment) Limited of U.K. The respondent assessee also borrowed from its shareholders in the same ratio as the equity share holding amount of Rs.57.09 crores from N.A. Basix SA and Rs.37.01 crores from Kier International Investment Limited. In the circumstances, the respondent had equity capital of Rs. 38.00 lacs and debt capital of Rs.9410 lacs. Thus, debt equity ratio worked out is to 248:1.*

5) *The respondent assessee paid interest of Rs. 5.73 crores on the aforesaid borrowing of Rs.57.09 crores and Rs.37.01 crores from NV Basix SA and Kier International (Investments) Limited respectively. However, the Assessing Officer disallowed the payment of interest in view of the Reserve Bank of India's approval letter dated 3/11/1998 granting approval to the assessee to do business in India. The approval letter dated 03/11/1998 specifically provided that India Branch Office will not borrow or lend from/to any person in India without specific permission of the Reserve bank of India. The Assessing officer further observed that in view of India Belgium Double Taxation Avoidance Agreement interest on monies paid by the Head Office to the branches was not allowable as a deduction.*

6) *In appeal, the Commissioner of Income Tax (Appeals) by an order dated 29/3/2007 upheld the order of the Assessing officer and disallowed the deduction on account of interest of Rs.5.73 crores paid to Joint Venture Partners. The Commissioner of Income Tax (Appeals) held that Article 7(3)(b) of the Double Taxation Avoidance Agreement forbids allowance of any interest paid to the head office by permanent establishment in India as a deduction. Further, the payment of interest also directly violates the conditions imposed by RBI in its letter dated 3/11/1998. Therefore, the order of the Assessing Officer was upheld.*

7) *However, the Tribunal allowed the respondent-assessee's appeal. During the course of the proceedings before the Tribunal the revenue contended that the borrowings on which the interest has been claimed as a deduction are in fact capital of the assessee and brought only under the nomenclature of loan for tax consideration. It was the case of the appellant-revenue before the Tribunal that debt capital is required to be re-characterized as equity capital. However, the Tribunal held that in India as the law stands there were no rules with regard to thin capitalization*

*so as to consider debt as an equity. It is only in the proposed Direct Tax Code Bill of 2010 that as a part of the General Anti Avoidance Rules it is proposed to introduce a provision by which a arrangement may be declared as an impermissible avoidance arrangement and may be determined by recharacterising any equity into debt or vice versa.*

*8) We find no fault with the above observations of the Tribunal. There were at the relevant time and even today no thin capitalization rules in force. Consequently, the interest payment on debt capital cannot be disallowed. In view of the above, the question (i) raises no substantial question of law and is therefore, dismissed."*

22. So, there is umpteen number of judgment declaring that transaction involving share application money cannot be recharacterized as international transaction of loan under Transfer Pricing provision.

23. Hon'ble Bombay High Court in case of *Pr. CIT vs. Aegis Limited in ITA No.1248 of 2016 dated 28.01.2019* held that in the absence of finding that the transaction was sham, the TPO could not have treated such transaction as a loan and charge interest thereon on notional basis. Coordinate Bench of the Tribunal in case of *Voltas Ltd. vs. DCIT, Range 8(3)(2), Mumbai in ITA No.2822/Mum/2017 & Ors.* in the identical facts and circumstances of the case held that, "*the payment of share application money cannot be treated as partly in the nature of interest free loans to the Associated Enterprises and as such, ALP adjustment based on that hypothesis is not legally sustainable*".

Operative part of the judgment is as under :-

*“3.5.7 Upon careful consideration of factual matrix as enumerated by us in the preceding paragraphs, the undisputed position that emerges is the fact that the assessee has advanced Share Application Money to one of its AE situated in Saudi Arabia with a view to acquire further stake in that entity. The entity has become wholly owned subsidiary of the assessee company during the month of January, 2009. The financial health of its AE was not good and the money was advanced with a view to infuse further capital in the AE and with a view to acquire controlling stake in its AE. The money has been utilized by its AE to pay-off business debts and to meet working capital requirements. Another undisputed fact is that ultimately the shares have been allotted to the assessee during December, 2015 after getting the desired regulatory approvals from concerned authority i.e. SAGIA. It is also undisputed fact that there was delay in the legal process which has been substantiated by the assessee, inter-alia, by furnishing email correspondences etc. The entirety of the facts and circumstances would demonstrate that the investment made by the assessee was for genuine business purpose and the stated transaction was not found to be a sham transaction, in any manner. Another fact is that whatever benefit would accrue to assessee's AE, they would indirectly accrue to the assessee since AE ultimately became wholly owned subsidiary of the assessee company. No doubt, there was inordinate delay in allotment of shares, nevertheless, the assessee was successful in explaining the delay in allotment of share and was able to demonstrate with evidences the circumstances which led to delay in allotment of shares. Therefore, re-characterization of this transaction as advance / loan by revenue authorities, in our considered opinion, was not correct approach and this transaction could not be equated with loan transactions. The Ld. DR has contended that the transactions have not been re-characterized as loan but the same has been benchmarked since certain benefits have accrued to AE by infusion of fund which must be shared with the assessee. However, we find that ALP of the transaction has been computed in similar manner as it would be computed for a loan transaction. Further as already noted, assessee's AE ultimately became wholly owned subsidiary of the assessee and therefore, whatever benefit would accrue to AE, the same would indirectly accrue to the assessee. Therefore, not convinced with the approach of lower authorities, we hold that no addition would be warranted on this account.*

.....

50. *In view of these discussions, as also bearing in mind entirety of the case, we are of the considered view that the authorities below were in error in treating the payment of share application money, as partly in the nature of interest free loans to the AEs, and, accordingly, ALP adjustment based on that hypothesis was indeed devoid of legally sustainable merits. We delete the impugned adjustment of Rs.19,15,45,943. The assessee*

*gets the relief accordingly. As we have decided this ground of appeal on the fundamental issue that the payment of share application money could not be partly treated as interest free loan to AE, we see no need to deal with other aspects of the matter.”*

24. Ld. DR for the Revenue by relying upon the order passed by the AO/CIT (A) contended that health of the AE needs to be looked into and it is not disclosed by the assessee company that if the loan was given and later on converted into equity. This contention of the ld. DR is not tenable for the reason that it is categoric case of the assessee company since very outset that funds were given to the subsidiary for business purpose and to have control over it. Moreover it was investment in equity.

25. In view of the decisions rendered by Hon'ble High Courts and coordinate Bench of the Tribunal discussed in the preceding paras, we are of the considered view that firstly, AO has no authority to re-characterize the transaction of making investment by the assessee company in equity shares of subsidiaries as a loan; secondly, OECD Guidelines also discourage restricting of legitimate business transaction; thirdly, when the AO has not come up with specific finding that the transaction in question is a sham transaction, he cannot treat the transaction of “capital infusion” by the assessee company as a loan and to charge the interest thereon on notional basis; and fourthly, in the absence of any specific

finding by the AO that any income has arisen from international transaction, TP provisions contained in Chapter-X of the Act do not apply. Section 92(1) of the act says that income arisen from international transaction is a condition precedent for application of Chapter-X of the Act. Consequently, we are of the considered view that addition made by the AO and confirmed by the Id. CIT(A) on account of arm's length price of value of interest receivable on loans outstanding of Rs.1,04,24,675/- in the name of Jaypee Singapore Pte Ltd. is not sustainable, hence ordered to be deleted. So, grounds no.10 to 13 are determined in favour of the assessee.

26. Resultantly, the appeal filed by the assessee is partly allowed.

**Order pronounced in open court on this 17<sup>th</sup> day of January, 2020.**

**Sd/-  
(R.K. PANDA)  
ACCOUNTANT MEMBER**

**sd/-  
(KULDIP SINGH)  
JUDICIAL MEMBER**

**Dated the 17<sup>th</sup> day of January, 2020.**

**TS**

Copy forwarded to:

- 1.Appellant
- 2.Respondent
- 3.CIT
- 4.CIT(A)-30, New Delhi.
- 5.CIT(ITAT), New Delhi.

**AR, ITAT  
NEW DELHI.**