

**IN THE INCOME TAX APPELLATE TRIBUNAL
“A” BENCH : BANGALORE**

**BEFORE SHRI N.V. VASUDEVAN, VICE PRESEIDENT
AND
SHRI PADMAVATHY S, ACCOUNTANT MEMBER**

ITA No.2515/Bang/2019
Assessment year : 2015-16

The Deputy Commissioner of Income Tax, Circle 7(1)(2), Bengaluru.	Vs.	Valdel Projects Corporation Pvt Ltd., No.2/1, Embassy Vogue, Palace Road, Vasanthnagar, Bengaluru – 560 052. PAN: AADCV 5652K
APPELLANT		RESPONDENT

Appellant by	:	Shri Narendra Sharma, Advocate
Respondent by	:	Shri Sankar Ganesh, Jt.CIT(DR)(ITAT), Bengaluru.

Date of hearing	:	24.05.2022
Date of Pronouncement	:	30.05.2022

ORDER

Per Padmavathy S., Accountant Member

This appeal of the revenue is against the order of the Commissioner of Income Tax (Appeals)-7 Bengaluru dated 30th day of September 2019 for the assessment year 2015-16.

2. The revenue raised the following grounds:-

1. The order of the CIT (A) is opposed to the law and facts of the case.

2. The learned CIT (A) erred in not appreciating the fact that the assessee has failed to establish that the borrowed capital has been utilised for its own business transactions other than advancing it to its sister concerns as interest free loans.
3. In the facts and circumstances of the case the learned CIT (A) erred in not appreciating that the facts of the case on hand are different from the case laws relied upon by the learned CIT (A) as the assessee has no other operations other than taking loans and advancement of loans to others whereas in the case law relied upon by the CIT (A) the assessee and its sister concerns were engaged similar business.
4. The appellant craves leave to add to alter or delete any of the grounds that may be urged at the time of hearing of the appeal.

3. The assessee is private limited company engaged in the business of real estate and construction activity and investment in IT parks STZ and commercial and residential real estate projects development. For the assessment year 2015-16 the assessee filed the return of income on 30th of September 2015 declaring a total loss of Rs.2,52,90,502. The case was selected for scrutiny and notice u/s. 143(2) of the Act was issued. The assessing officer completed the assessment u/s. 143(3) where the AO made a disallowance of Rs. 2,70,14,120 towards interest cost u/s.36(1)(iii) on the ground that the funds borrowed have not been utilised for the purpose of business of the assessee. On further appeal the CIT(A) allowed the appeal in favour of the assessee. The revenue is in appeal against the order of the CIT (A).

4. During the assessment year 2015-16 the assessee has claimed total finance cost of Rs. 2,70,17,905. The said the interest is paid to L&T infrastructure Finance Co Ltd towards the issue of 15% secured nonconvertible redeemable debentures by the assessee. During the

assessment year 2012-13 the assessee has issued 5000 non-convertible redeemable debentures of Rs.1,00,000 each to L&T infrastructure Finance Co Ltd totaling to Rs. 50,00,00,000 @ 15% per annum. The said proceeds were in turn advanced to the subsidiary of the assessee wide agreement dated 31st of May 2011 as under :-

M/s Valdel Infra (India) Private Limited	–	Rs.35 crores
M/s Valdel Real Estate Private limited	–	Rs.15 crores

5. During the course of hearing the assessing officer noticed that the assessee has borrowed loans and is paying interest whereas the investment made by the assessee in its subsidiaries does not carry any income. Before the AO the assessee submitted that it had issued the debentures for utilising the funds mobilised through such issue towards its business purposes and the amounts were in turn advanced to its downstream companies for legitimate business purposes for reasonable interest cost. Due to adverse and unfavourable business conditions the downstream companies were unable to perform as expected and were not in a position to service the interest cost or recognise any interest income during the year under assessment. The assessing officer did not accept the submissions of the assessee and disallowed the interest paid by the assessee u/s. 36(1)(iii) stating that the assessee instead of utilising the funds borrowed for the purpose of generating income, it is advancing without any income and that the funds borrowed not utilised for the purpose of business.

6. Aggrieved, the assessee preferred an appeal before the CIT(A). The assessee submitted before the CIT (A) that the assessee is an investment company and one of the objects of the assessee is acquisition, subscription and holding shares in various companies and thus in order to protect its

business interest it has advanced monies to its subsidiaries as and when found expedient for business purposes. The assessee submitted a copy of the memorandum of Association in support of the nature of the assessee's business. The CIT(A) deleted the disallowance made by the assessing office by accepting the contention of the assessee that the subsidiaries are in the similar business as that of the assessee and the assessee it operates through its subsidiary companies for achievement of its strategic business objects. The CIT(A) has also stated that the advancement of loan by the assessee to its subsidiaries therefore cannot be said to be devoid of any business purpose and that the assessee not to have received interest on its advanced cannot be held against the assessee to deny its claim of deduction of interest payment on borrowings.

7. Aggrieved at the revenue is in appeal before the Tribunal. The learned DR submitted that the assessee has borrowed the funds by issuing debenture with interest rate of 15% and the funds so borrowed have been lent to its subsidiaries at the rate of 15% is probably loan agreement entered into with the subsidiaries. The learned DR submitted that the assessee was charging interest in the initial period of loan however did not charge interest during the year under consideration. The learned DR drew our attention to the balance sheet and profit and loss account (page 13 and 14 of paperbook) to submit that the assessee is an investment company and not in the business of real estate.

8. The learned AR reiterated the submissions made before the lower authorities. The learned AR submitted that the main reason for disallowing the interest by the assessing officer was that the funds borrowed have been used for non-business purposes. This the learned AR argued that is not factually correct given that the assessee has invested the funds borrowed in its subsidiaries and has given financial assistance for the purpose of the business of the subsidiary companies as a matter of

strategy, investment and long-term perspective to benefit from the long-term growth of the subsidiary companies and not for immediate return. The financial assistance given is in the interest of commercial expediency. The only condition laid down in section 36(1)(iii) of the Act is that interest should be paid on a loan that is used for the purpose of business and since the assessee has used the borrowed funds for the purpose of business the interest paid on such borrowed funds should be allowed u/s. 36(1)(iii). The learned AR submitted that the assessee not charging interest on loan given to its subsidiaries has got no relevance for allowability of interest u/s. 36(1)(iii) and in this regard relied on the decision of the Supreme Court in the case of *S A builders Ltd vs CIT(A) (2007) 288 ITR 1(SC)*.

9. We heard the rival submissions and perused the material on record. The assessee has entered into a debenture subscription agreement dated 31st of May 2011 with L&T infrastructure finance company limited whereby the investor has agreed to provide financial assistance of Rs.50,00,00,000 to the assessee by subscription to unlisted secured redeemable nonconvertible debentures. The assessee is the holding company of various entities within Veldel group operating in the sector of real estate and infrastructure projects through its wholly owned subsidiaries namely Veldel Real Estate Private Limited (VREL) and Veldel Infra (India) Private Limited (VIPL). Clause 3 of the above agreement talks about use of investment amount, which is reproduced below: -

“The company and promoters have represented to the investor that any part of the investment amount to be dispersed by the investor shall be used as loans to the company’s subsidiaries which will invest in and IT industrial parks, special economic zones and commercial and residential real estate projects and more particularly defined in the business plan (defined below). Based on such representation the company and the promoters, the investor (L&T) has agreed to provide the company with the investment amount. The company and the promoters agree that

out of the total investment amount of Rs.35,00,00,000 will be given as unsecured loan to VIPL and Rs.15,00,00,000 will be given as unsecured loans to VREL for investment in projects in accordance with the loan agreements to be executed between the company and VIPL and the company and VREL”.

10. As per clause 4 of the agreement, the assets of the subsidiaries namely VIPL and VREL and also the various properties developed by VIPL and VREL are given as security to the investor (L&T). From the analysis of the various clauses of the agreement it is clear that the assessee has borrowed the funds to be lent as loans to its subsidiaries towards developing various real estate and infrastructure projects. We also notice that the CIT(A) in the order has analysed the various clauses of the Memorandum of Association [MoA] of the assessee which states the objects of the company and that the funds borrowed have been used for the purpose of the business of the assessee through its subsidiaries. The relevant clauses of the MoA are reproduced below:-

“Main object of the assessee

To purchase lease sale exchange or otherwise acquire and dealing all kinds of real estate in India and elsewhere and to form layout, construct, erect and maintain building, colonies, townships, commercial complexes

To plan setup develop own construct operate maintain sell purchase or exchange otherwise lease upgrade or acquire business parks industrial parks, software technology parks, biotechnology parks, engineering and consultancy parks.

Objects incidental/ancillary to attainment of main object

Subject to the provisions of the Act to invest, apply for and acquired or otherwise employ monies belonging to, entrusted to or at the disposal of the company with without security upon terms as may be brought proper and from time to time verify such transaction in a manner company may think fit.

To borrow or raise money with or without security or to receive money on deposit interest otherwise in such a manner as the company may think fit and in particular by the issue of debentures vendor stock convertible into shares of this or any other company.

To carry on business which may seem to the company capable of being conveniently carried on in connection with the above objects or any of them calculated directly or indirectly to enhance the value of or render profitable any of the properties or right of the company.

11. From a reading of the relevant clauses of the Memorandum and the terms of the agreement, it is clear that the assessee has invested the funds raised through issue of debentures in the subsidiaries for commercial expediency and is used for the business purpose of real estate through the subsidiaries. In this regard we notice that the Supreme Court in the case of *S A Builders Ltd (supra)* has dealt with a similar issue and has held as under:-

“25. The expression “commercial expediency” is an expression of wide import and includes such expenditure as a prudent businessman incurs for the purpose of business. The expenditure may not have been incurred under any legal obligation, but it is allowable as a business expenditure if it was incurred on grounds of commercial expediency.

31. It is true that the borrowed amount in question was not utilised by the assessee in its own business but had been advanced as interest free loans to its sister concern. However in our opinion that fact is not really relevant. What is relevant is whether the assessee advanced such amount to its sister concern as a measure of commercial expediency.

35. We wish to make it clear that it is not our opinion that in every case interest on borrowed loan has to be allowed if the assessee advances it to a sister concern. It all depends on the facts and circumstances of the respective case. For instance, if the directors of the sister concern utilised the amount advanced to it by the assessee for their personal benefit, obviously it cannot be said that such money was advanced as a measure of commercial expediency. However money can be said to be advanced to a sister concern for commercial expediency in many other circumstances (which need not be enumerated here). However where it is obvious that a holding company has a deep interest in its subsidiary and hence if the holding company advances borrowed money to a subsidiary and the same is used by the subsidiary for some business purpose the assessee would in our opinion ordinarily be entitled to deduction of interest on its borrowed loans.”

12. In this case the assessee has borrowed funds and invested the same in the subsidiaries who have utilised these funds for the purpose of real estate and infrastructure development. The assessee has given the loans to its subsidiaries out of the borrowed funds with the purpose to earn future income within the framework of its main objects and for commercial expediency. For the purpose of claiming deduction u/s. 36(1)(iii) of the Act the conditions to be satisfied are that the expenditure in question should be in the nature of interest and the borrowing on which such interest is paid should have been for the purpose of business. The given case the assessee has indeed used the borrowed funds for the purpose of its business by investing/loaning to its subsidiaries to be used for real estate and infrastructure development. Hence considering the facts of the case and following the principles laid down by the Hon'ble Supreme Court in the case of *S A Builders Ltd (supra)*, we hold that the assessee is entitled for deduction of interest u/s. 36(1)(iii) of the Act. The appeal is allowed in favour of the assessee.

13. In the result, the appeal by the revenue is dismissed.

Pronounced in the open court on this 30th day of May, 2022..

Sd/-
(N V VASUDEVAN)
VICE PRESIDENT

Sd/-
(PADMAVATHY S)
ACCOUNTANT MEMBER

Bangalore,
Dated, the 30th May, 2022.

/Desai S Murthy/

Copy to:

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR, ITAT, Bangalore.

By order

Assistant Registrar
ITAT, Bangalore.