

**INCOME TAX APPELLATE TRIBUNAL
MUMBAI 'H' BENCH, MUMBAI**

**[Coram: Pramod Kumar (Vice President)
and Rahul Chaudhary (Judicial Member)]**

ITA No.6089/Mum/2019
Assessment Year: 2013-14

Steller Films Pvt. Ltd.

102-103, A/4, Lok Nirman Tower, Dr. Ambedkar Road,
Khar (W), Mumbai 400 052 [PAN: AAQCS7991B]

..... Appellant

Vs.

**Assistant Commissioner of Income Tax, Circle 16(1)
Mumbai**

.....Respondent

Appearances:

Lalchand Chaudhari for the appellant

Milind Chavan for the respondent

Date of concluding the hearing : 17.06.2022

Date of pronouncement the order : 15.09.2022

O R D E R

Per Pramod Kumar, VP:

1. By way of this appeal the assessee appellant has challenged the correctness of the order dated 15th July 2019, passed by the learned CIT(A) in the matter of assessment under section 143(3) of the Income Tax Act 1961, for the assessment year 2013-14.

2. In ground no 1, the assessee has raised the following grievance:-

1 The CIT(A) was not justified in confirming the action of the AO in disallowing legal fees of Rs. 2,286,520 paid to the retainer advocates firm for taking care of litigation without appreciating the fact that these expenditures were incurred for exclusively for the purpose of its routine business.

3. To adjudicate on this grievance, only a few material facts need to be noted. The assessee before us is a company engaged in the business of cinema photographic films. During the course of the scrutiny assessment proceedings, the Assessing Officer noticed that the assessee has claimed legal and professional fee of Rs. 27,40,834/- but “since it is not an expenditure co-relatable to any income credited in the profit and loss account during year under consideration” the said expenses were disallowed. The plea of the assessee that these amounts were paid to the lawyers to represent the assessee before Hon’ble Bombay High Court as there was dispute with respect to film “Sher” with Ashthivinayak Cinevision, the entity which was to produce the same under arrangements with the assessee, was rejected. Aggrieved, assessee carried the matter in appeal before the CIT(A) but without complete success. Aggrieved, assessee is in further appeal before us.

4. We have heard the rival contentions, perused the material on record and duly considered facts of the case in the light of the applicable legal position.

5. We find that the learned CIT(A) has retained the disallowance of Rs. 22,86,520/- for the short reason that these expenses pertain to a film which may not be released. In our considered view, this approach is clearly erroneous because as long as it is not in dispute that the expenses are incurred wholly and exclusively for the purpose of business, as indeed is the position in this case, there is no occasion for disallowance of such expense. Whether the film is released or not, or whether it turns out to be a dud project, as in this case, is wholly irrelevant. We, therefore, uphold the plea of the assessee and direct the Assessing Officer to delete this disallowance of Rs. 22,86,520/-. The assessee gets the relief accordingly.

6. Ground no 1 is thus allowed.

7. In ground no 2, the assessee has raised the following grievance:-

2 The CIT(A) was not justified in confirming the action of the AO in disallowing service charges of Rs. 19,66,300 paid to the agent involved in the contract for the film ‘Sher’ with film producing company. The CIT(A) failed to appreciate that having failed to release the film ‘Sher’, the appellant has abandoned the said film permanently and thus the expenditure incurred in relation thereof is business loss/revenue expenditure.

8. So far as this disallowance is concerned, the Assessing Officer, during the course of the scrutiny assessment proceedings, made the disallowance of Rs. 19,66,300 on account of service charges by observing as follows:-

5. Disallowance of service charges:

During the course of assessee proceedings it is seen that the assessee has paid Rs.19,66,300/- under the head legal & professional fees to Abrianna Advertising and Marketing Service Pvt. Ltd. Further, the assessee has submitted invoice No. AAPL/139/2012-2013 dated 15.03.2013 which reads as "Being the charges @ 1% for the services towards getting the agreement signed for the movie 'Sher' with Shree Ashtavinayak Cine Vision Ltd. at Rs. 19,66,300/-.

5.1. As noted above, film 'Sher' has not been released and same is under production. In this regard, authorized representative of the assessee was asked to give justification why amount paid to Abrianna Advertising and Marketing Service Pvt. Ltd. should not be added as WIP project "SHER" as the same is related to project. In reply the authorized representative of the assessee vide letter dated NIL at point 7 in para 2 submitted as under:

“..... 7. Rs. 19.66 lacs were paid to Abrianna Advertising and Marketing Service Pvt Ltd for getting the agreement signed with Shree Ashthavinayak Cinevision. The same cannot be treated as a part of WIP since the same was agreed and paid after the movie was ready.....

5.2. Thus, it is crystal clear from the preceding paras of this order that the film being under production. Therefore, an amount of Rs. 19,66,300/- claimed as expenses by the assessee is hereby disallowed and added to the total income of the assessee. Penalty proceedings u/s. 271(1)(c) of the Income-tax Act, 1961 is initiated separately for furnishing inaccurate particulars of income.

9. Aggrieved, assessee carried the matter in appeal before the CIT(A) but without any success. Learned CIT(A) confirmed the disallowance and justified the disallowance as below:-

6.2 Ground No. 2: Vide this ground of appeal appellant is agitated against disallowance of 719,66,300/- on account of service charges paid to Abrianna Advertising & Marketing Services Pvt. Ltd. In para 5.1 of assessment order the AO has stated that film 'Sher' had not been released and the same was under production. The AO asked the assessee to explain as to why the amount paid to Abrianna Advertising & Marketing Services Pvt. Ltd. should not be added as WIP project "Sher" as the same was related to project. In response to this, the assessee company filed a written submission. The Ld. AO was not satisfied with the explanation of the assessee company, therefore, he disallowed the amount of 719,66,300/- claimed as expense and added it to the total income of the assessee.

6.2.1 During the course of appellate proceedings, the appellant claimed that the film was complete and as such the expenses should be allowed. As per Rule 9A deduction for cost of production of a feature film is allowed in the previous year in which it is certified for release by the Board of Film Censors. Since in appellant's case, film was not certified for release by the Board of Film Censors, deduction of above said expense of service charges amounting to Rs. 19,66,300/- cannot be allowed. Hence, I upheld the view taken by AO in this regard and reject this ground of appeal of the assessee. Therefore, this ground of appeal is dismissed.

10. The assessee is not satisfied and is in further appeal before us.
11. We have heard the rival contentions, perused the material on record and duly considered facts of the case in the light of the applicable legal position.
12. We find that, as subsequent developments turned out, there is no dispute that the film 'Sher' was finally abandoned and it was never released. The entire expenditure incurred on the said project, including these expenses, constitute business loss and are allowable as such. We, therefore, uphold the plea of the assessee, and, accordingly, direct the Assessing Officer to delete the impugned disallowance of Rs. 19,66,300. The assessee gets the relief accordingly.
13. Ground no 2 is thus disallowed.
14. In ground no 3, the assessee has raised the following grievance:-

3. *The CIT(A) was not justified in confirming the action of the AO in disallowing interest expenditure of Rs. 157,50,000 paid in respect of funds borrowed in the normal course of business. The CIT(A) failed to appreciate that the borrowing in the normal course of business are deductible expenditure when the appellant has abandoned the said film permanently and thus the expenditure incurred in relation thereof is business loss/revenue expenditure.*

15. So far as this disallowance is concerned it was also made by the Assessing Officer for the short reason that the related in this year, and, accordingly, the interest payment was to be capitalized. The relevant observations of the Assessing Officer are as follows:-

7. *Disallowance of interest paid as per 9A:*

It is seen that the assessee has debited of Rs. 5,03,90,235/- as interest expenses under the head financial expenses at not 14 of profit & loss account on certain interest bearing funds borrowed of Rs. 40,31,51,211/-. It is seen from the record that the assessee has given advance of Rs. 17,50,00,000/- to M/s. Shree Ashtavinayak Cine Vision P. Ltd. out of the borrowed funds. During the course of the assessment proceedings, the authorised representative of the assessee was asked to show cause as to why the interest expenses claimed should not be disallowed as the funds borrowed are used for the film production cost which is work in progress project "Sher" at Rs.17,50,00,000/-, as the same is of capital in nature and not released in the year under consideration on the basis of the provisions mentioned under Rule 9A.

7.1. *In response to the same, the authorized representative of the assessee has filed the letter stated therein that:*

"As already submitted that in FY 2011-12, assessee had issued ORCDs to Cinema Capital Venture fund for Rs.30 crores carrying interest @ 9%. The interest paid against these debentures was Rs.2.70 crores. The debentures were issued immediately after the company was incorporated and the funds were used to start the commercial operations. In the absence of these funds, the assessee would not have started the operations.

On going through the above details, your goodself will also appreciate that there is no interest expenses which can be disallowed/capitalized. The interest paid during the year was towards loan taken for projects which were executed during the year and income from which has been offered to tax.

7.2. Hence, considering the above facts, on the basis of Rule 9A of the Income-tax Rules, 1962 which reads as under:

"(1) In computing the profits and gains of the business of production of feature films carried on by a person (the person carrying on such business hereafter in this rule referred to as film producer), the deduction in respect of the cost of production of a feature film certified for release by the Board of Film Censors in a previous year shall be allowed in accordance with the provisions of sub-rule (2) to sub-rule (4).

Explanation: In this rule,

(i) Board of Film Censors means the Board of Film Censors constituted under the Cinematograph Act, 1952 (37 of 1952);

(ii) cost of production, in relation to a feature film, means the expenditure incurred on the production of the film, not being

(a) the expenditure incurred for the preparation of the positive prints of the film; and

(b) the expenditure incurred in connection with the advertisement of the film after it is certified for release by the Board of Film Censors:]

[Provided that the cost of production of a feature film, shall be reduced by the subsidy received by the film producer under any scheme framed by the Government, where such amount of subsidy has not been included in computing the total income of the assessee for any assessment year.]

(2) Where a feature film is certified for release by the Board of Film Censors in any previous year and in such previous year,

(a) the film producer sells all rights of exhibition of the film, the entire cost of production of the film shall be allowed as a deduction in computing the profits and gains of such previous year; or

(b) the film producer

(i) himself exhibits the film on a commercial basis in all or some of the areas; or (ii) sells the rights of exhibition of the film in respect of some of the areas; or

(iii) himself exhibits the film on a commercial basis in certain areas and sells the rights of exhibition of the film in respect of all or some of the remaining areas, and the film is released for exhibition on a commercial basis at least [ninety] days before the end of such previous year, the entire cost of production of the film shall be allowed as a deduction in computing the profits and gains of such previous year.

(3) Where a feature film is certified for release by the Board of Film Censors in any previous year and in such previous year, the film producer

(a) himself exhibits the film on a commercial basis in all or some of the areas;
Or

(b) sells the rights of exhibition of the film in respect of some of the areas; or

(c) himself exhibits the film on a commercial basis in certain areas and sells the rights of exhibition of the film in respect of all or some of the remaining areas, and the film is not released for exhibition on a commercial basis at least ninety] days before the end of such previous year, the cost of production of the film in so far as it does not exceed the amount realized by the film producer by exhibiting the film on a commercial basis or the amount for which the rights of exhibition are sold or, as the case may be, the aggregate of the amounts realized by the film producer by exhibiting the film and by the sale of the rights of exhibition, shall be allowed as a deduction in computing the profits and gains of such previous year; and the balance, if any, shall be carried forward to the next following previous year and allowed as a deduction in that year."

7.3. Therefore, in view of the above, since the film is not released in the year under consideration, hence the claim of assessee of interest on loan is disallowed as it falls within the preview of Rule 9A of the Income-tax Rules, 1962. The assessee has to capitalize the interest incurred in the cost of production of movie "Sher". Hence, in view of the above, interest on loan works out to Rs.1,57,50,000/- (i.e. Rs.17,50,00,000/- @ 9%) is hereby disallowed as capital in nature and added back to the total income of the assessee. Penalty Proceedings u/s. 271(1)(c) of Income-tax Act, 1961 are separately initiated for furnishing inaccurate particulars of income.

16. Aggrieved, assessee carried the matter in appeal but without any success. Learned CIT(A) confirmed the disallowance on the basis of following reasons:-

6.3 Ground No. 3: Vide this ground of appeal appellant is agitated against disallowance of interest on loan amounting to 71,57,50,000/-. In para 7 of the assessment order, the Ld. AO noticed that the assessee gave advance of 717,50,00,000/- to M/s Shree Ashtavinayak Cine Vision P. Ltd. out of borrowed funds. In this regard, AO asked the assessee to show cause as to why the interest expenses claimed should not be disallowed as the funds borrowed were used for the film production cost which was work in progress project "Sher" and expenses for an amount of 717,50,00,000/- were capital in nature. Further, the Ld. AO has stated that since the film was not released in the year under consideration, hence the claim of assessee of interest on loan was disallowed as it falls within the preview of Rule 9A of the Income Tax Rules, 1962. The assessee had to capitalize the interest incurred in the cost of production of movie "Sher". Hence in view of above, AO worked out interest on loan at 71,57,50,000/- (i.e. 9% of 717,50,000,000/-) and the same was disallowed as capital in nature and added the same to the total income of the assessee company.

6.3.1 As discussed in para 6.2.1 of this order, as per Rule 9A deduction for cost of production of a feature film is allowed in the previous year in which it is certified for release by the Board of Film Censors. Since in appellant's case, film was not certified for release by the Board of Film Censors, deduction of interest as stated above cannot be allowed and needs to be capitalized. In this regard, I uphold the view of AO, however, as stated by appellant interest should not have

been worked for the entire year but on basis of funds used during the year, considering the actual dates of payment. I, therefore, direct the Assessing Officer to recompute the amount of disallowance based on number of days funds were used during the year and not for the entire year. Hence, this ground of appeal is partly allowed.

17. The assessee is aggrieved and is in appeal before us. In the course of hearing before us, assessee also filed a brief note as follows:-

The assessee is in the business of Film Financiers and Distributors. In the course of its business, the assessee used to get films produced from contract producers for a definite budget (Price). Feature films are stock in trade of the assessee costs of which are fully deductible against the revenue generated. In this case, the assessee had hired a producer who was producing the feature film namely 'Sher' with star cast of M/s. Sanjay Dutt and Vivek Oberoi and being directed by Mr. Soham Shah and granted a trading advance of Rs. 17.50 Crores under an agreement date 22/02/2012. (Page 3-23 of Paper Book).

As per terms of the agreement, the contract producer Shree Ashtvinayak Cinevision Limited (SACVL) was to produce the film 'Sher' and deliver to the assessee latest by the end of December, 2012. Till the film was produced and delivered, a lien in favour of the assessee was created on the under production film 'Sher' to secure the money so advanced. In case of failure of the contract producer (SACVL), the assessee was entitled to get full refund of the advance of Rs. 17.50 Crore with interest @ 21% per annum. (Para 2.1 and Para 2.5 of Agreement on page 6 of the Paper book).

The AO has disallowed 1,57,50,000 being part of the interest expenditure by working the disallowance @ 9% (Flat) on the amount of advance Rs. 17.50 Crore. The AO also disallowed Rs. 22,86,520 being part of the legal fees paid to defend the rights of the assessee in this film and also disallowed Rs. 19,66,300 paid by the assessee to the agent involved in this film financing contract by assuming that these expenditure are in respect of a Film which is primarily a Capital asset.

Hon'ble CIT (A) granted part relief and directed the AO to recompute disallowance of interest based on actual dates of payment of Rs. 17.50 Crores. However, in principle confirmed the order of the AO.

Primary assumption of the AO that a film is a capital asset is incorrect. Infact, a feature film is only a stock in trade. All expenditures incurred on a film are revenue expenditures and are allowed to be deducted in the year of release of film like trading goods. Hon'ble Mumbai bench of the ITAT has also taken this view in the matter of ACIT v. A K Films (P) Ltd [2014] 41 taxmann.com 512; [2015] 152 ITD 538 (Mumbai). In para 4 of the decision, Hon'ble bench has discussed the issue in detail and took a view that a feature film is a stock in trade and all expenditure to produce a film are revenue expenditure.

The contract producer (SACVL CIN L92110MH2001PLC133759) failed to produce the film and complete the project. The film therefore could not be released and the project has been abandoned. SACVL which was a famous film producer is facing number of criminal and insolvency suits and is now under liquidation. As per MCA website, this company has not held its AGM after 30/12/2013 and is presently under liquidation. The assessee could not recover any

By order

*Assistant Registrar/Sr. PS
Income Tax Appellate Tribunal
Mumbai benches, Mumbai*