

IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH "B", MUMBAI
BEFORE SHRI ABY T VARKEY, JUDICIAL MEMBER AND
SHRI GAGAN GOYAL, ACCOUNTANT MEMBER
ITA No. 3088/Mum/2018 (A.Y. 2013-14)
ITA No. 3089/Mum/2018 (A.Y. 2014-15)

DCIT, CC-3(1),

Room No. 1924, Air India Building,

19th Floor, Nariman Point,

Mumbai-400021.

..... Appellant

Vs.

M/s Nirmal Lifestyle (Pune) P. Ltd.

3rd Floor, Multiplex Building,

LBS Marg, Mulund (W),

Mumbai-400080.

PAN: AACCN4986H

..... Respondent

Appellant by : Dr. Mahesh Akhade - CIT(DR)

Respondent by : Sh. Bhadresh Doshi

Date of hearing : 26/07/2022

Date of pronouncement : 20/10/2022

ORDER

PER GAGAN GOYAL, A.M:

These appeals by the Revenue are directed against the order of Ld. Commissioner of Income Tax(Appeals)-51, Mumbai [hereinafter referred to as ['CIT(A)'] vide common orders dated 13.02.2018 passed under section 143(3) r.w.s. 153(A) of the Income Tax Act, 1961 (hereinafter referred to as ['the Act'] for

the Assessment Years (AY) 2013-14 & 2014-15 respectively. We shall take up ITA No. 3088/Mum/2018 for A.Y. 2013-14 as lead case. 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) erred in directing to compute only the proportionate interest out of the total interest expenditure of Rs.9,20,66,434/- and reduce this proportionate interest from the closing WIP of the assessee".*

2. *"On the facts and in the circumstances of the case and in law the Ld. CIT(A) erred in directing the AO to compute only the proportionate loan processing fees out of the total loan processing fee of Rs. 2,76,40,560/- and reduce this proportionate loan processing fee from the Closing WIP shown by the assessee'*

The appellant craves to leave, to add, to amend and / or to alter any of the ground of appeal, if need be.

The appellant, therefore, prays that on the ground stated above, the order of the Ld.CIT(A)-51, Mumbai, may be set aside and that of the Assessing Officer restored."

2. In ITA No. 3089/Mum/2018 (AY-2014-15), 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) erred in directing to compute only the proportionate interest out of the total interest expenditure of Rs.13,91,29,852/- and reduce this proportionate interest from the closing WIP of the assessee".*

The appellant craves to leave, to add, to amend and / or to alter any of the ground of appeal, if need be.

The appellant, therefore, prays that on the ground stated above, the order of the Ld.CIT(A)-51, Mumbai, may be set aside and that of the Assessing Officer restored."

3. Brief facts of the case are that the assessee-company is engaged in the business of Construction of Residential and Commercial Projects has filed its return of income for A.Y. 2013-14 originally on 26.09.2013 declaring total income

of Rs. Nil. A search and survey action under section 132 & 133A of the Act was carried out on 23.10.2013 in the case of M/s Nirmal Lifestyle Ltd. and its associated concerns, subsidiaries and residences of main persons. Assessee-company was also searched under section 132 of the Act. Accordingly, notice under section 153A of the Act issued in response to this letter, assessee filed a letter dated 09.12.2015 requesting to treat the original return filed as return filed under section 153A of the Act.

4. During assessment proceeding, it was noticed that no business activity was carried out by the company. In the relevant A.Y. assessee had other income of Rs.2, 04, 950/-. As against this, expenses viz.- Direct expenses relating to purchase of land such as brokerage etc, Personal expenses, Administrative expenses and financial expenses such as Band charges, interest paid etc. aggregating to Rs. 13,11,86,981/- have been incurred. As the project was not started, these expense were transferred to 'Work-in-progress' A/c and return was filed showing Total Income at Rs. Nil. During the course of assessment proceedings, it was noticed that company has secured loan of Rs. 72, 08, 14,316/- out of this assessee has given interest free loan to group company M/s Nirmal Manor Pvt. Ltd. amounting to Rs. 61,67,87,380/-.

5. During the year under consideration, assessee incurred finance cost of Rs. 11,97,06,994/- (Rs. 9,18,35,041/- on secured loan + Rs. 2,78,71,953/- on other loans). AO worked out interest @ 18% on interest free loans given to group companies amounting to Rs. 11,10,21,728/- and added the same to the income of the company under the head "Income from Other Sources".

6. Other than the issue of interest assessee has incurred loan processing charges to obtain secured loan from M/s Future Capital Holdings Ltd. amounting to Rs. 3,41,20,000/-. Out of this loan processing charges, Rs. 2, 76, 40,560/- were also disallowed and added to the income of the assessee on the same ground as mentioned (supra). Assessee being aggrieved with the order of A.O, filed an appeal before the CIT (A)-51, Mumbai.

7. Ld. CIT(A) partly allowed the appeal of the assessee vide para-5.8, 5.9, 5.10 & 5.11 on page no. 11 & 12 of CIT(A)'s order. The relevant extract of Ld. CIT (A)'s order is reproduced here-in-below:

"5.8 In view of the aforesaid discussion, the action of the AO of making an addition of Rs. 11.10.21.728/ being the notional interest income computed by applying a rate of 18% on the interest free loan advanced to M/s. Nirmal Lifestyle Ltd., a related concern, cannot be sustained

5.9 However, it is observed that the assessee has claimed an aggregate Interest expenditure of Rs. 9, 20, 66,434/- (Rs 9, 18, 35,041/- + Rs 2, 31,393/-) which has been included in the WIP. The proportionate interest expenditure on interest bearing funds which have been diverted to give the said interest free loan to M/s Nirmal Manor P Ltd. cannot be allowed as a deduction while computing the Closing WIP of the assessee. The ratio of decision of Hon'ble Supreme Court in the case of SA Builders (supra) that if a loan is given to a subsidiary company on account of commercial expediency, no disallowance out of interest expenditure can be made, cannot be applied in the case of the assessee since the borrower i.e., Nirmal Manor P Ltd. is not a subsidiary of the assessee and as such it has no investments in the borrower company and therefore the fortunes of the assessee are in no way connected with that of the borrower company. Since, the assessee is maintaining a common pool of funds, the proportionate interest attributable to the interest free loan given to M/s. Nirmal Manor P Ltd. can be computed by adopting the same principles of formulae given in Rule 8D(2)(ii) which is for determining the interest attributable to the investments which yield exempt income. The AO is directed to accordingly compute the proportionate interest out

of the total interest expenditure of Rs. 9,20,66,434/- and reduce this proportionate interest from the closing WIP of the assessee.

Disallowance of loan processing fees of Rs 2, 76, 40,560/- on the loan availed

5.10 As regards the issue of disallowance of loan processing fees, the AO has made this addition since the loan availed by paying the loan processing fee was diverted for the purpose of giving interest free loan to M/s Nirmal Manor P Ltd. and therefore the said fee cannot be allowed as a business expenditure. The assessee contends that the loan processing fee has been paid to avail loan for its business activities and is therefore allowable as a deduction.

5.11 As noted earlier, the assessee's revenue from operations have not commenced till the end of the relevant year. The entire expenditure claimed by the assessee including the loan processing fees of Rs. 2, 76, 40,560/- has been included in the closing WIP. It is also a fact that the assessee has diverted part of its interest bearing funds for the purpose of giving interest free loans to M/s. Nirmal Lifestyle Ltd. Therefore, the loan processing fees attributable to the interest bearing funds diverted for the said loan to M/s. Nirmal Lifestyle Ltd. cannot be allowed as business expenditure. Since, the assessee is maintaining a common pool of funds, the proportionate loan processing fees attributable to the interest bearing funds which were diverted for giving interest free loans to M/s. Nirmal Lifestyle Ltd. can be computed by adopting the same principles of the formulae given in Rule 8D (2)(i) which is for determining the interest attributable to the investments which yield exempt income. This proportionate loan processing fee out of the total loan processing fee of Rs. 2, 76, 40,560/- cannot be allowed as a business expenditure. However, since revenue from operations have not commenced till the end of the relevant year and the entire expenses incurred are included in the closing WIP, only the closing WIP can be reduced by the proportionate loan processing fees related to the interest free loan advanced to M/s Nirmal Manor P. Ltd and no separate addition can be made. The AO is directed to accordingly compute the proportionate loan processing fees out of the total loan processing fee of Rs. 2,76,40,560/- and reduce this proportionate loan processing fee from the Closing WIP shown by the assessee."

8. We have gone through the order of AO, order of Ld. CIT (A) and submissions of the assessee along with case laws relied upon. Assessee relied upon following judicial pronouncements along with its submissions as under:

“5.1 During the course of appellate proceedings, the Ld AR of the assessee submitted as under:

"During the year under consideration, the Appellant holds secured loan of Rs 72,08,14,316/- Loan processing fees of Rs. 2,76,40,560/- and also interest amounting to Rs 9,18,35,041/- were also incurred for the same during the year. The appellant has shown the same as finance cost incurred during the year The assessee company has given interest free loans to group company- Nirmal Manor Pvt. Ltd. aggregating to Rs. 61, 67, 87,380/- whereby the said advance was just a normal diversion to the holding company for temporary period due to non-usability of the said funds on account of problem of clearance permission of the land possessed by the assessee company upon which construction activities were to be started. The Ld. Assessing Officer has overlooked these crucial facts and considered interest @18% on the said amount advanced to Nirmal Manor Pvt. Ltd. working out to Rs. 11,10,21,728/- deemed to be income earned from the loan and the same has been taxed under Income from Other Sources Apart from this the above mentioned loan processing fees of Rs. 2,76,40,560/- has also been disallowed whereby we would want to mention that sufficient time and reasonable opportunity was not provided, to prove the legality of the said transaction, which is against the principal of Natural Justice.

Explanation on Grounds of Appeal

The Appellant is in the Business of Builders and Developers ie Construction of Residential and Commercial Complexes in Mumbai A Search and Survey Action was carried out u/s 132 & 133A of the Income Tax Act, 1961 on 23 October, 2013 on Nirmal Group of Companies where Appellant being part of the Group Concern was covered by the Search proceedings. Accordingly the Ld. A.O. issued notice u/s 153A of the Income Tax Act, 1961 and asked the Assessee to file the Return of Income against the same. The Assessee, in response to the said notice filed a Reply on 10.12 2015 stating that the Return filed u/s 139(1) shall be treated as Return filed u/s 153A of the Income Tax Act, 1961.

The Search and Survey operations were extensively carried out at the Registered Office Addresses of the entire group (including the Appellant). Site addresses, Residential Premises of the Directors and Key Managerial Personnel. The Income Tax Authorities found various loose papers in the course of their Search

Proceedings in the premises where the Search Operations were conducted and Statements u/s 132(4) of the Act were recorded of the various persons in whose premises Search operations were carried out Various Papers, CD's, data in the pen-drives were seized by the Income Tax Authorities and explanation regarding each and every seized material was sought by the Income Tax Authorities and recorded in the form of Statements u/s 132(4) of the Act.

In the instant case, the issue is whether the Ld. A.O. was justified on the facts of the case and in law to add the national Interest Income @ 18% of the Loan advanced to M/s Nirmal Manor Pvt. Ltd. which is a Group Concern of the Appellant.

The Appellant being in the Business of Construction of Flats as stated earlier, had a requirement of substantial amount of Funds so as to infuse liquidity in the Business of the Appellant and facilitate the smooth functioning of the Activates to achieve the ultimate Business Objective i.e. Construction of Flats to sell them to the Target Customers and earn profits out of the same.

The Appellant in order to satisfy its Capital Requirements had taken a Secured Loan from M/s Future Capital Holding's Limited with an initial limit of Rs. 50 Crores which was further extended to Rs. 82 Crores during the year under consideration. Further, the Appellant had paid a sum of Rs. 2, 76, 40,560/- on the said Loan as Loan Processing Fees in order to get The Loan Sanctioned and Cleared for the stated Purpose. We are herewith submitting the copy of Sanction Letter for your ready reference from Page 28831 of the paper Book.

The Directors of the Appellant had planned that the said Loan taken shall be utilized for the Purpose of Construction and Development of Residential Flats at Mulund and accordingly they had applied for various permissions for clearing the title of the Land and also to start the construction activities on the said Land. However, since the Appellant was not able to get the permissions sought for the commence the Business Activities the Loan Funds already availed by the Appellant were lying idle and the Interest Cost of the Appellant was piling up on the idle funds which was proving prejudicial to the Financial Position of the Company Hence, in order to counter the situation, the Directors of the Appellant Company decided to divert some of the Funds to the Group concern i.e. M/s Nirmal Manor Pvt. Ltd. which is involved in the Business of Short Term as well as Long Term Financing so as to cover up for the Interest Cost which was being borne by the Appellant Company without the actual utilization of the Funds.

The said Loan was advanced to M/s Nirmal Manor Pvt. Ltd. without charging any Interest since ultimately the Funds were lying with the Group Concern and were being utilized for the Business purpose of the concern. The above arrangement not only provided a cover for the unnecessary interest Cost incurred by the Appellant but also facilitated Commercial Expediency by employing the Funds within the Group Concern. It is also a settled Law and a well-accepted fact that if the funds are diverted for the purpose of Commercial Expediency then the disallowance u/s 36 (1)(iii) is not warranted.”

“S.A. Builders Ltd. Vs. Commissioner of Income Tax (Appeals), (Supreme Court)

The High Court as well as the Tribunal and other income-tax authorities should have approached the question of allowability of interest on the borrowed funds from the above angle. In other words, the High Court and other authorities should have enquired as to whether the interest-free loan was given to the sister company (which is a subsidiary of the assessee) as a measure of commercial expediency, and if it was, it should have been allowed. 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, yet it is allowable as business expenditure if it was incurred on grounds of commercial expediency.

The Apex Court in the above case held that where the Funds had been diverted with a view to facilitate Commercial Expediency the disallowance u/s 36(1)(ii) of the Act was not warranted. Apart from that the Apex Court also casted a responsibility on the High Court as well as the Lower Authorities that they should have inquired whether the Loan was given as a measure of Commercial Expediency and if so disallowance was not tenable in law which in the instant case was not done by the Ld AO Hence, disallowance shall be deleted.

Bright Enterprises Pvt. Ltd. Vs. CIT, High Court of Punjab & Haryana

The Assessing Officer's view that the advance was not for business purposes as the appellant had no business dealings with the sister company is erroneous. Commercial expediency in advancing loans does not arise only on account of there being transactions directly between the holding company and the subsidiary company or between the group companies inter se. The two companies may even be in a different line of business. It would make no difference. It would still be commercially expedient for one group company to

advance amounts to another group company, if, for instance, as a result thereof the former benefits. In the present case, as we have already demonstrated, there would be a direct benefit on account of the advance made by the appellant to its sister company if the same improves the financial health of the sister company and makes it a viable enterprise. We hasten to add that it is not necessary that the advance results in a positive tangible benefit. So long as the amount is advanced with that view in mind or with any other commercially expedient view in mind that is sufficient.

The Hon'ble High Court of Punjab & Haryana observed that for commercial expediency it is not necessary that there shall be direct transactions between the group concerns and that the company to whom the loans is advanced should be in the same line of business as that of the Assessee. Hence, keeping in the view of the Court, the Addition of notional Interest shall be deleted.

Further, with regards to the Loan Processing Fee of Rs. 2,76,40,560/- it was a necessary revenue expenditure which had to be incurred by the Appellant so as to avail the Loan which was taken for the purpose of the Business i.e. Project Financing. The Ld. A.O. disallowed the said expenditure citing that the said expenditure was not incurred for the purpose of Business and the expenditure remained unexplained. However, since the expenditure was in relation to the Loan availed for the purpose of Business it shall be allowed since it had direct nexus with the Business of the Appellant. The Ld. AO failed to appreciate the fact that the Loan Funds were given as a measure of Commercial Expediency keeping in mind the Business Prudence and ultimately the said Loan was to be repaid by the Group Concern as and when the Business Activities of the Appellant would commence smoothly.

Moreover, any kind of expenditure incurred by the Appellant in order to procure funds by whatever name called (Loan Processing Fees in the instant case) was to be allowed as revenue expenditure since it had direct nexus with the Business Activities as it was impossible for the Appellant to procure loan without incurring such expenditure. Further, the Loan procured was ultimately a liability which was to be repaid from the business receipts on the Appellant and no advantage or benefit accrued to the Appellant from the said Loan apart from it being infusing the liquidity in the business.

Similar view was taken in the following Judicial Pronouncements-

India Cements Ltd. Vs. Commissioner of Income Tax, (Supreme Court)

A loan obtained cannot be treated as an asset or advantage for the enduring benefit of the business of the assessee. A loan is a liability and has to be repaid and, it is erroneous to consider a liability as an asset or an advantage. The nature of the expenditure incurred in raising a loan would not depend upon the nature of purpose of the loan. A loan may be intended to be used for the purchase of raw material when it is negotiated, but the company may, after raising the loan, change its mind and spend it on securing capital assets. Therefore, the purpose for which the new loan was required was irrelevant to the consideration of the question whether the expenditure for obtaining the loan was the revenue expenditure or capital expenditure. In the result, the expenditure in question was not in the nature of capital expenditure and was laid out or expended wholly or exclusively for the purpose of the assessee's business.

The Honourable Supreme Court in the above case held that, nature of expenditure incurred for procuring the Loan had no relevance with the purpose of procuring the Loan and the same shall be allowed as a Revenue Expenditure.

CIT Vs. Super Spinning Mills Ltd. (High Court of Madras)

Where during the year of account the assessee obtained sanction for a term loan of Rs. 820 lakhs from the IDBI and while availing of the above loan, the assessee incurred a sum of Rs. 8.20 lakhs towards "front-end fee payment" at the rate of 1 per cent on the loan amount. Held that without paying the above said amount, the IDBI might not have sanctioned the loan amount for setting up the new unit. Here the amount was paid only for obtaining the loan and, hence, the same did not bring into existence any asset of an enduring nature. If interest paid on borrowed amount could be held to be revenue expenditure, one failed to see how the present amount incurred for obtaining a loan for setting up of a new unit could be regarded as capital payment it was the condition precedent for obtaining the loan and also it was in the nature of processing fees for the bank to release the loan incurred for the purpose of the business and, hence, the same was only revenue expenditure.

The Hon'ble Madras High Court in the above case has taken a view that the expenditure which has been incurred for the purpose of procuring Loan without which the Bank would not have sanctioned the Loan was allowable as a Business Expenditure.

Without Prejudice to all the above facts of the case and the contentions placed by the Appellant we would like to draw your kind attention to the fact that the Ld

A.O, initiated the Assessment Proceedings u/s. 153A of the Income Tax Act, 1961 as a consequence to the Search conducted u/s 132 of the Act. However, the additions as made by the Ld. A.O. have no connection whatsoever with the Search Proceedings since no incriminating material was found so as to justify the Addition of Notional Interest Income and Loan Processing fees. There is no evidence placed on record by the Ld. A.O. which corroborates with the Addition and that it has any relation with the findings made at the time of the Search.

1) Commissioner of Income-Tax Continental Warehousing V. Corporation (Nhava Sheva) Ltd. (High Court of Bombay) [2015]

"True it is that the assessment which has to be made in pursuance of the notice is in relation to the six years. An order will have to be made in that regard. While making the order the income or the return of income filed for all these assessment years is to be taken into account. A reference will have to be made to the income disclosed therein. However, the scope of enquiry, though not confined as held by the High Court of Karnataka, it essentially revolves around the search or the requisition under section 132A as the case may be."

As per the italicised part the Court gave its view on the issue of nexus between incriminating material found during the course of search and addition made at the time of assessment u/s 153A of the Income Tax Act, 1961 is pronounced in the favour of the Assessee. The fact prevailing in the case of Appellant and aforesaid judicial pronouncement is that no incriminating material related to notional interest or unexplained expenditure was found during the course of search action so no addition can be made on the said issue.

2) Commissioner of Income-Tax v. Kabul Chawla given by Delhi Tribunal and recently upheld by High Court of Delhi [2015]

"The present appeals concern AYS, 2002-03, 2005-06 and 2006-07. On the date of the search the said assessments already stood completed. Since no incriminating material was unearthed during the search, no additions could have been made to the income already assessed."

The above judicial pronouncement also took a view that was taken by Hon'ble High Court of Bombay in case of Continental Warehousing Corporation (Nhava Sheva) Ltd and so we request your good self to take into view the facts prevailing in the case of Appellant.

The same has also been upheld in below judicial pronouncements:

1) Principal Commissioner of Income-Tax v. Meeta Gutgutia (High Court of Delhi)[2017]

2) Anil Mahavir Gupta v. Assistant Commissioner of Income-Tax (ITAT Mumbai) [2017]

3) Atul Barot v. Deputy Commissioner of Income-Tax (ITAT Mumbai) [2014]

4) Om Shakthy Agencies (Madras) (P.) Ltd. v. Deputy Commissioner of Income-Tax (ITAT Chennai)[2016]."

9. We have gone through the submissions of the assessee and judicial pronouncements relied upon. We found force in the contentions of the assessee on two folds i.e. (1) Expenditure claimed by assessee not debited to the Profit & Loss A/c, hence, the same cannot be disallowed and treated as income & (2) No interest has ever been received by the assessee, in that case no notional income can be added back in the hands of assessee. Proportionate disallowance of interest and loan processing fee, out of the total amount debited to WIP by the assessee is justified on the given set of facts and judicial pronouncements relied upon by the assessee.

10. The order of Ld. CIT (A) dealt the whole issue in a very just and fair manner. In his order, he tried to balance both the sides keeping in view the principles of commercial expediency and accounting norms. We found the order passed by Ld. CIT (A) as sustainable and no interference from our side is warranted. In the result, we agree with the findings and formulas given by the Ld. CIT (A). As we are sustaining the order of Ld. CIT (A), Ground No.1 & 2 raised by the Revenue is dismissed.

11. In the result, appeal filed by the Revenue is dismissed.

ITA No. 3089/Mum/2018 (A.Y. 2014-15)

12. In this appeal, Revenue raised only one ground relating to Interest Expenditure. The ground raised in this appeal is similar to what we have decided in ITA No. 3088/Mum/2018 for A.Y. 2013-14 (Ground No.1). As the facts and law applicable is exactly the same, our findings in ITA No.3088/Mum/2018 for A.Y. 2013-14 is applicable mutatis mutandis here also. No separate adjudication is required. In the result, Ground No.1 raised by the Revenue is dismissed in this appeal also.

13. **In the result, appeal filed by the Revenue is dismissed.**

Order pronounced in the open court on 20th day of October, 2022.

Sd/-
(ABY T VARKEY)
JUDICIAL MEMBER

Sd/-
(GAGAN GOYAL)
ACCOUNTANT MEMBER

Mumbai, दिनांक / Dated: 20/10/2022

SK, Sr.PS

Copy of the Order forwarded to:

1. अपीलार्थी / The Appellant ,
2. प्रतिवादी / The Respondent.
3. आयकर आयुक्त (अ) / The CIT(A)-
4. आयकर आयुक्त CIT
5. विभागीय प्रतिनिधि, आय.अपी.अधि., मुंबई / DR, ITAT, Mumbai
6. गार्ड फाइल / Guard file.

BY ORDER,

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(Dy. /Asstt. Registrar)
ITAT, Mumbai