

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

BEFORE SHRI GEORGE GEORGE K., JUDICIAL MEMBER
AND
SHRI LAXMI PRASAD SAHU, ACCOUNTANT MEMBER

ITA No.1171/Bang/2022
Assessment year : 2014-15

RNS Infrastructure Limited, 7 th Floor, Naveen Complex, No.14, M.G. Road, Trinity Circle, Bangalore – 560 001. PAN: AACCR 7165G	Vs.	The Deputy Commissioner of Income Tax, Range 2(3), Bangalore.
APPELLANT		RESPONDENT

Appellant by	:	Shri Shreesh Kumar Hegde, CA
Respondent by	:	Shri P. Suresh Rao, Addl.CIT(DR)(ITAT), Bengaluru.

Date of hearing	:	26.04.2023
Date of Pronouncement	:	17.05.2023

ORDER

Per Laxmi Prasad Sahu, Accountant Member

This is the second round of appeal before the ITAT by the assessee against the order of the CIT(Appeals)-11, Bengaluru dated 27.10.2022 DIN: ITBA/APL/M/250/2022-23/ 1046481087(1) for the assessment year 2014-15.

2. The sole issue involved out of the grounds raised in this appeal is disallowance of interest expenditure of Rs.2,14,35,676 under proviso to section 36(1)(iii) of the Income-tax Act, 1961 [the Act].

3. Briefly stated facts are that the assessee filed return of income on 22.9.2014 declaring total income at Rs.8,80,66,421. The case was selected for scrutiny and statutory notices were issued to the assessee. During the course of assessment proceedings, the AO noted that the assessee has given advances of Rs. 24,13,56,764 to its sister concern, M/s. Naveen Hotels Ltd. for purchase of land and the average interest at Rs. 2,14,35,676 has been paid on the OD facility by the assessee. The advance for land was made from the OD a/c/Current a/c/CC a/c. The AO observed that the advance paid to Naveen Hotels Ltd. (sister concern) was capital in nature, because the loan advanced to Naveen Hotels was for purchase of land and it was not put to use during the impugned assessment year. Therefore the interest expenditure should be capitalized instead of claiming it as revenue expenditure. Accordingly the same was added to the income of the assessee.

4. The CIT(Appeals) upheld the order of the AO in the second round of set aside proceedings before him also. Aggrieved, the assessee is in appeal before the Tribunal.

5. The Id. AR reiterated the submissions made before the lower authorities and filed written synopsis which is as under:-

“GROUND — 3 : DISALLOWANCE OF INTEREST UNDER
FIRST PROVISIO TO SECTION 36(1)(iii)

"3. The learned CIT(A) has erred by holding that the learned Assessing Officer has rightly invoked the 'proviso to sec.36(1)(iii)' of the Act and thereby disallowing the interest expenditure of Rs.2,41,35,676 on the facts and circumstances of the case. Further, the learned CIT(A) failed to appreciate that the proviso to section 36(1) can be invoked only when the borrowed funds are utilized for acquisition of the capital asset on the facts and circumstances of the case."

Facts of the case:

6. The learned Assessing Officer has disallowed interest expense of Rs. 2,41,35,676 relating to bank overdraft facilities claimed as revenue expenses. The Appellant had paid an advance of Rs.24,13,56,764 for land of M/s. Naveen Hotels Ltd. The Appellant has made these payments from overdraft and cash credit facilities obtained from the bank. The said advance will be receivable by the Appellant and such amount will not be capitalized in the books of account of the Appellant. The advance is not a capital expenditure in the books of the Appellant attracting the proviso to section 36(1)(iii) of the Act in the instant case. Thus, the said advance has not resulted in any capital assets or the Appellant has capitalized any asset in the books of accounts. The relevant portion of the proviso to section 36(1)(iii) of the Act has been provided below for Your Honors ease of reference:

"Other deductions.

36. (1) The deductions provided for in the following clauses shall be allowed in respect of the matters dealt with therein, in computing the income referred to in section 28

(i)

(ii)

(iii) the amount of the interest paid in respect of capital borrowed for the purposes of the business or profession :

Provided that any amount of the **interest paid, in respect of capital borrowed for acquisition of an asset** (whether capitalised in the books of account or not); for any period beginning from the date on which the capital was borrowed for acquisition of the asset till the date on which such asset was first put to use, shall not be allowed as deduction."

(Emphasis provided)

Treatment by learned Assessing Officer and learned Commissioner of Income Tax (Appeals):

7. The learned Assessing Officer was of the view that the Appellant has incurred interest expenses on the overdraft and cash credit facilities. He further held that, the interest expenses could have been allowed only if the asset (land) would have been put to use for the purpose of business. He disallowed the interest holding that the interest pertaining to this capital expenditure cannot be claimed as revenue expenditure and adopted the 10 percent as rate of interest and accordingly disallowed the proportionate interest amounting to Rs. 2,41,35,676. The learned Assessing Officer has added back such interest income to the total income of the Appellant.

8. The learned CIT(A) has confirmed the addition of interest holding that the proviso to section 36(1)(iii) are applicable to the Appellant. The Appellant most humbly submits that the advance has been given to the sister concern. The said advance will be receivable by the Appellant and such amount will not be capitalized in the books of account of the Appellant. The advance is not a capital expenditure in the books of the Appellant attracting the proviso to section 36(1)(iii) of the Act in the instant case. Thus, the proviso to section 36(1)(iii) is not applicable to the facts of the case.

9. In view of the above, the Appellant prays before Your Honors to hold that the proviso to section 36(1)(iii) is not applicable in the instant case and direct the lower authorities to delete the addition of Rs. 2,41,35,676 made under the provisions of section 36(1)(iii) of the Act.

GROUND — 5 : DISALLOWANCE OF PROPORTIONATE INTEREST

"5. The learned CIT(A) is not justified in upholding the extent to which the interest expenditure is disallowed by the learned assessing officer on proportionate on the facts and circumstances of the case."

10. The Appellant most humbly states that the proviso to section 36(1)(iii) requires the interest paid in respect of capital borrowed for acquisition of an asset to be disallowed for any period beginning from the date of which the capital was borrowed for acquisition of the asset till the date on which such asset was first put to use shall not be allowed as deduction.

11. In the instant case, the learned Assessing Officer has disallowed the interest on proportionate basis. The learned Assessing Officer failed to appreciate that the Appellant has not borrowed any form of facility from the Banks for advancing the amount to the sister concern. The borrowing of loan in relation to acquisition of asset is one of the primary condition for the applicability of Proviso to Section 36(1)(iii) of the Act. Further, the Proviso requires that portion of the interest to be disallowed incurred/paid from the date of borrowing till the asset is first put to use. There is no satisfaction of these conditions in the orders passed by the lower authorities.

12. The Appellant has obtained two cash credit facilities from Canara Bank and State Bank of India respectively which have been duly disclosed in Note No. 2.6 of the financial statements. Your Honors attention is drawn to Page No.128 of the paper book wherein the short term borrowings has been disclosed in the financial statements. Thus, on perusal of the financial statements, it is apparent that the Appellant has not taken any loan for making advance to the sister concern.

13. In view of the above, the Appellant most humbly prays before Your Honors to hold that the orders passed by the lower authorities are not tenable in law and to direct the lower authorities to delete the addition of interest of Rs. 2,14,35,676 made under the provisions of section 36(1)(iii) of the Act.

WITHOUT PREJUDICE,

GROUND — 4 : FREE FUNDS ADVANCED TO SISTER CONCERN:

"4. The learned CIT(A) has erred by not holding that the Appellant had advanced the free funds on the facts and circumstances of the case."

14. The Appellant has made the payment to sister concern out of the interest free cash available with the Appellant. The Appellant most humbly states that the finding of the learned Assessing Officer that the payments has resulted in over drawals and negative balance increased from time to time leading to charging of OD/CC interest by the bank is factually incorrect. The Appellant has utilized the interest free funds available in making the advance to Naveen Hotels Ltd.

15. In case, the Appellant has utilized the overdraft and cash credit facility in making the land advance to Naveen Hotels, the cash outflow from financing activity should have been higher by such amount over and above the cash generated from operating activity. The Appellant has generated cash of Rs. 43,04,92,050.88 from the operating activities and cash outflow from financing activities amounted to Rs. 38,75,13,394.03 during the year under consideration. Your Honors reference is drawn to page number 145 of the paper book for the cash flow statement. Further, the position of the current assets and current liability at (page no. 122 of the paper book) has been provided below for Your Honors kind attention.

Sr. No.	Particulars	Amount in Rs. As at 31/03/2014	Amount in Rs. As at 31/03/2013
1.	Current Assets	243,18,42,490	309,84,33,214
2.	Current Liabilities	144,29,38,740	196,07,01,114

16. The entire current liabilities of Rs. 144,29,38,740 outstanding as at 31/03/2014 has been invested in the current assets of the Appellant. The Appellant most humbly states that, while sanctioning the working capital limit, the banks will take necessary care in ensuring that the facilities are not utilized for other than business purpose. The bank will determine the drawing power on a month on month basis by obtaining monthly work done certificates/stock and receivable statements, work orders etc excluding all kinds of long term loans and advances.

17. Further, the Appellant most humbly states that the finding of the learned Assessing Officer further confirmed by the learned Commissioner of Income Tax (Appeals) that the payments has resulted in over drawals and negative balance increased from time to time leading to charging of OD/CC interest by the bank is factually incorrect. The Appellant has utilized the interest free funds available in making the advance to Naveen Hotels Ltd. The summary of the interest free funds available with the Assessee as at the end of the period are as under:

Sr. No.	Particulars	Amount in Rs. As at 31/03/2014	Amount in Rs. As at 31/03/2013
3.	Share Capital	63,00,00,000	63,00,00,000
4.	Reserves and Surplus	91,84,56,786	87,12,72,995
	Total	1,54,84,56,786	1,50,12,72,995

18. Thus, the entire land advance for Naveen Hotels are made from the interest free funds available with the Assessee. Kindly refer page 122 of the paper book for balance sheet for Your Honors ease of reference.

19. The Appellant wishes to place reliance on the decision of the Hon'ble Jurisdictional Tribunal in the case of ACIT V/s. IDEB Projects Private Limited in ITA No.1531(Bang)/2012 where the Hon'ble Tribunal has held as under:

"12. Regarding Grounds 5 to 9 in respect of deletion of disallowance of interest of Rs. 23,25,95,267/- u/s 36 (1) learned DR of the revenue supported the assessment order and learned AR of the assessee supported the ITA No. 1531/B/2012 order of CIT (A). He also submitted that as per the revised Balance Sheet on page 17 of the paper book, the own interest free funds are to the extent of Rs. 151.44 Crores on 31.03.2009 and Rs. 179.63 Crores on 31.03.2008. Then he drawn our attention to page 11 of the assessment order and pointed out that as per the A.O., the interest free advances to sister concern a on 31.03.2009 is only Rs. 128.89 Crores and on 31.03.2008 only Rs. 136.12 Crores. He submitted that own interest free funds on both these dates i.e. 31.03.2009 and 31.03.2008 is in excess of interest free advances and therefore, no disallowance of interest is justified. He placed reliance on the tribunal order rendered in the case of M/s. Kems Auto

Components Ltd. vs. DCIT in ITA No. 100/B/2014 dated 16.09.2016 (Copy Filed) and pointed out that in that case, the tribunal followed the Judgment of Hon'ble Bombay High Court rendered in the case of CIT vs. Reliance Utilities & Power Ltd., 313 ITR 540.

13. We have considered the rival submissions. In view of the facts noted above as per which, own interest free funds on both these dates i.e. 31.03.2009 and 31.03.2008 is in excess of interest free advances and by respectfully following the tribunal order cited by the learned AR of the assessee having been rendered in the case of M/s Kems Auto Components Ltd. vs. DCIT (Supra) and the Judgment of Hon'ble Bombay High Court rendered in the case of CIT vs. Reliance Utilities & Power Ltd. (Supra), we decline to interfere in the order of CIT (A) on this issue. These grounds are rejected."

The copy of the order has been provided at Page No. 24 to 35 of the legal paper book for Your Honors ready reference. Kindly refer para 13 of the case law for the relevant portion of the observation of the Hon'ble Tribunal. The ratio laid down by the Hon'ble Tribunal squarely covers the facts of the Appellant. Thus, the interest free funds are much higher than the amount of land advance paid to Naveen Hotel in the instant case of the Appellant.

20. The Appellant wishes to place reliance on the decision of Hon'ble Supreme Court in the case of CIT V/s. Reliance Industries Limited in Civil Appeal No. 10 of 2019 dated 02/01/2019 wherein the Hon'ble Apex Court has held as under:

"Insofar as the first question is concerned, the issue raises a pure question of fact. The High Court has noted the finding of the Tribunal that the interest free funds available to the assessee were sufficient to meet its investment. Hence, it could be presumed that the investments were made from the interest free funds available with the assessee. The Tribunal has also followed its own order for Assessment Year 2002-03. In view of the above findings, we find no reason to interfere with the judgment of the High Court in regard to the first question. Accordingly, the appeals are dismissed in regard to the first question."

The copy of the order has been provided at Page No. 06 to 08 of the legal paper book for Your Honors ready reference. Kindly refer para 7 of the case law for the relevant portion of the observation of the Hon'ble Supreme Court. The order of judgment of the Hon'ble High Court of Bombay has been enclosed at Page No. 09 to 17 of the legal paper book for Your Honors ready reference. Kindly refer para 33 of the case law at page 13 for the relevant portion of the observation of the Hon'ble High Court.

21. The Appellant places reliance on the judgement of Hon'ble Bombay High Court in the case of CIT V/s. Reliance Utilities & Power Ltd [2009] 178 Taxman 135 (Bombay) at para 10 has held that if there are funds available, both, interest-free and overdraft and/or loans taken, then a presumption would arise that investments would be out of interest-free funds generated or available with company. The copy of the order has been provided at Page No. 01 to 05 of the legal paper book for Your Honors ready reference. Kindly refer para 8 to 10 of the case law for the relevant portion of the observation of the Hon'ble High Court. The relevant portion of the judgment has been reproduced below for Your Honours ease of reference:

"The principle therefore would be that if there are funds available both interest-free and overdraft and/or loans taken, then a presumption would arise that investments would be out of the interest-free fund generated or available with the company, if the interest-free funds were sufficient to meet the investments. In this case this presumption is established considering the finding of fact both by the CIT (Appeals) and ITAT."

22. In view of the above, the Appellant prays before Your Honors to uphold that learned Commissioner of Income Tax (Appeals) has erred in holding that the proviso to section 36(1)(iii) of the Act are applicable to the facts of the case. Further, it is prayed before Your Honors to uphold that learned Commissioner of Income Tax (Appeals) has erred in holding that the Appellant has utilised the borrowed funds in advancing the amount to the sister concern.

23. the Appellant prays before Your Honors to uphold that the interest free funds have been utilised in advancing the funds to

the sister concern M/s. Naveen Hotels Limited and accordingly direct the lower authorities to delete the interest added under the proviso to section 36(1)(iii) of the Act in the instant case.

24. We request Your Honors to take the above on record for Your Honors kind consideration and gracious favourable orders for the substantial cause of justice and equity in the instant case.”

6. In addition to the above, the Id. AR strongly submitted that proviso to section 36(1)(iii) is not applicable in the present facts of the case and submitted that assessee had sufficient internal accruals during the impugned assessment year which is evident from the cash flow statements which is part & parcel of the financial statements. He also submitted that the assessee had earlier given advances pf Rs.53.93 crores on which no expenditure has been charged. The AO has considered only the advances given during the impugned assessment year. He relied on the following case laws:-

- i) CIT v. Reliance Utilities & Power Ltd. [2009] 178 Taxman 135 (Bombay)
- ii) CIT v. Reliance Industries Ltd. [2019] 102 taxman.com 52 (SC)
- iii) CIT v. Reliance Industries Ltd. [2017] 86 taxman.com 24 (Bombay)
- iv) CIT v. Shapoorji Pallonji & Co. Ltd. [2020] 117 taxmann.com 625 (Bombay)
- v) IEDB Projects Pvt. Ltd. v. ACIT (ITAT Bang.)

7. On the other hand, the Id. DR relied on the orders of lower authorities and submitted that the CIT(Appeals) has rightly confirmed the order of the AO after examining the details. It is evident from the orders of the lower authorities that the assessee has given advances to its sister concern from the OD a/c /CC a/c / Current a/c which clearly

indicates that the assessee had no sufficient own funds for giving advances and there was no debit balance of loan accounts. The lower authorities have rightly observed that the advances were given from the OD/CC/Current A/cs. He further submitted that the land purchased by Naveen Hotels Ltd. was not put to use during the impugned assessment year, therefore it should be capitalized. He also submitted that the case laws relied on the by the Id. AR are distinguishable on the present facts of the case.

8. After hearing both the sides, perusing the entire material on record and the orders of the lower authorities, we note that the assessee had advanced loans of Rs.24,13,56,764 to Naveen Hotels Ltd. which is a sister concern for the business purpose for purchase of land and interest has been paid by the assessee on the loan account. The AO proportionately disallowed the interest by holding that the interest should be capitalized as per proviso to section 36(1)(iii) because the assets were not put to use during the impugned assessment year. On going through the ledger account of Naveen Hotels in the books of the assessee company, it is noticed that the interest free funds have been given on various dates on piece-meal basis and the amount has also been received back from the sister concern on different dates, but no interest has been charged on the advances. We further note from the cash flow statement placed at page 145 of PB that there is net cash generated from operating activity of Rs.43,04,92,050.88 and there is opening cash and cash equivalent balance of Rs.16.68 crores and closing cash and cash equivalent of Rs.17.44 crores. Since the internal

cash accruals from operations are more than the interest free funds advanced to the sister concern for business purposes, it cannot be said that the interest bearing loan funds had been utilized by the assessee for the purpose of giving interest free advances over the years to its sister concern, Naveen Hotels Ltd. In view of this factual finding and relying on the judgment of Hon'ble Supreme Court in the case of *Munjil Sales Corporation v. CIT* reported in [2008] 168 Taxman 43 (SC) order dated 19.2.2008, we hold that proviso to section 36(1)(iii) is not applicable in the present case. Accordingly, we set aside the order of the CIT(Appeals) and delete the addition.

9. In the result, the appeal of the assessee is allowed.

Pronounced in the open court on this 17th day of May, 2023.

Sd/-

(GEORGE GEORGE K)
JUDICIAL MEMBER

Sd/-

(LAXMI PRASAD SAHU)
ACCOUNTANT MEMBER

Bangalore,

Dated, the 17th May, 2023.

/Desai S Murthy/

Copy to:

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

By order

Assistant Registrar
ITAT, Bangalore.