

IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCH 'C', BANGALORE

BEFORE SHRI. N. V. VASUDEVAN, JUDICIAL MEMBER

AND

SHRI. ABRAHAM P. GEORGE, ACCOUNTANT MEMBER

I.T.A No.608/Bang/2015
(Assessment Year : 2010-11)

M/s. Stanley Lifestyle P. Ltd,
No.12/7, Sham Rao Compound,
Mission Road, Bangalore 560 027
PAN : AALCS3766P

..Appellant

v.

Principal Commissioner of Income-tax - 6,
Bangalore

..Respondent

Assessee by : Shri. V. Srinivasan, CA
Revenue by : Shri. Sunil Kumar Agarwala, JCIT

Heard on : 03.08.2015
Pronounced on : 14 .08.2015

ORDER

PER ABRAHAM P. GEORGE, ACCOUNTANT MEMBER :

In this appeal filed by assessee, it assails an order dt.19.03.2015 of Pr.CIT-6, Bengaluru, passed u/s.263 of the Income-tax Act, 1961 ('the Act'in short).

02. Assessee states in its ground that there was no error in the order passed by the AO, warranting a rectification u/s.263 of the Act, by the Pr. CIT.

03. Facts apropos are that assessee had filed return for the impugned assessment year declaring income of Rs.3,23,08,650/-. Assessment was completed by the AO u/s.143(3) on 26.03.2013. As per the assessee it had furnished details called by the AO which inter alia included advances to its related concerns shown in its balance sheet. Further as per the assessee it had also produced details of loans which were called by the AO. Assessment was completed u/s.143(3) of the Act, wherein the disallowances made was confined to employees' contribution to PF. Thereafter on 24.02.2014 Pr.CIT issued a show cause notice to the assessee stating that assessee had given advance of Rs.4,80,09,440/- to two companies for which no interest was charged by it. As per the Pr. CIT, assessee had, on the other hand paid interest of Rs.4,01,14,554/- on loans taken from banks. Further as per the Pr. CIT, the amounts borrowed on interest were utilised for giving loans to related parties, and, AO failed to make corresponding disallowance of interest. To the above show cause notice, assessee filed a reply on 21.04.2014. In such reply assessee stated that the details of the advances given to the two related concerns were produced before the AO. Assessee also explained that no interest bearing funds were utilised for giving such loans. As per the assessee it had share capital and free reserves far in excess of the amounts advanced to related parties and therefore presumption of the Pr. CIT that advances were given out of the interest bearing funds was incorrect. Assessee also pointed out that major part of advances given to the related parties comprised of Rs.4,79,69,399/- given to M/s. Stanley Retail Ltd, ('SRL' in short). As per the assessee, SRL was promoted by the same persons

who were the share holders of the assessee and was engaged in retail selling of goods manufactured by the assessee. Again as per the assessee sums given by it were used by SRL for establishing a retail out let to sell goods manufactured by the assessee. Thus according to the assessee, even if borrowed funds were presumed to have been utilised for giving advances, interest was allowable based on the principles of commercial expediency.

04. However, the Pr. CIT did not accept the above contentions of the assessee. According to the Ld. CIT, net current assets of the assessee which was Rs.31.72 crores as on 31.03.2009 had gone up to Rs.32.08 crores as on 31.03.2010. There was no change in the gross block of fixed assets. Thus according to him, part of the shareholders funds and borrowed funds were used in financing the current assets. Net current assets having gone up, there was a corresponding cost incurred for financing such current assets. According to him, abstract calculations based on figures given in balance sheet at the opening and the closing of the year, by itself would not give correct results. As per the CIT, assessee had taken loan of Rs.1,00,00,000/- from Engineering Design & Solutions India P. Ltd, another sum of Rs.75 lakhs from one Lakshmi Narayan Vyapaar and Rs.4,65,86,000/- from one Sunil Suresh which were all squared up during the same previous year, except for a small sum due to Sunil Suresh. According to him, such additional loans which were taken during the relevant previous year though squared up during the same previous year, would have gone to finance the investments in the sister concern. Interest cost on the

working capital had gone up from Rs.2.83 crores to Rs.3.57 crores. Therefore, as per the CIT the explanation of the assessee that interest-free advances were only used for giving the advances to the related concerns could not be believed. In so far as the claim of commercial expediency was concerned, CIT was of the opinion that any advantage to SRL would be beneficial only to its promoters and not to the assessee. As per the CIT, assessee did not derive any advantage more than what it could have got if such retail outlets were opened by third parties. When third parties were also doing the same type of business in the same territory as per the CIT, there was no commercial expediency in giving such huge advances to SRL for opening a new outlet. According to him AO had not examined the issue of interest-free advances as required under law. He directed the AO to disallow Rs.4,01,14,554/- out of total interest charged by the assessee to its P & L account considering the prime lending rate of SBI. Modification of the assessment order to this extent was ordered.

05. Now before us, Ld. AR strongly assailing the order of the Pr. CIT, submitted that two conditions necessarily had to be satisfied for invoking the provisions of Section 263 of the Act. According to him, there ought to be an error in the order of AO and such order had to be prejudicial to the interests of the Revenue. According to him, these two conditions were not satisfied. Placing reliance on letter dt.04.12.2013 written by assessee to the AO during the course of assessment proceedings, Ld. AR submitted that assessee had given details of other advances which were called for by the AO. According to Ld.

AR, AO had considered this aspect while framing the assessment order. In any case according to him, assessee had share capital, share application money and reserves totalling to Rs.10.41 crores as on 31.03.2009 and Rs.13.01 crores as on 31.03.2010. As against this, the total loans given to the two sister concerns totalled to Rs.4,80,09,443/-. Thus, as per the Ld. AR, assessee had substantial own funds for making the investments. Once own funds were there, as per the Ld. AR, the presumption should always be that investments had gone out of such own funds and not from interest bearing funds. As per the Ld. AR, it was not necessary to show one to one nexus. Reliance was placed on the judgment of Hon'ble Bombay High Court in CIT v. Reliance Utilities and Power Ltd [(2009) 313 ITR 340]. Further, as per the Ld. AR once assessee had shown that it had substantial own funds with it and it had answered related queries, then the presumption that there was error in the order of the AO was incorrect. There was no evidence relied on by the Pr. CIT which could show that order of the AO was prejudicial to the interests of the Revenue. Relying on the judgment of Bombay High Court in the case of Reliance Utilities and Power Ltd (supra), Ld. AR submitted that assessee had given a reply to the show cause notice of the Pr. CIT and demonstrated that it had sufficient own funds much higher than the loans given to its sister concerns. Thus according to him, the order of AO could not be considered as prejudicial to the interests of Revenue. Reliance was also placed on the judgment of Hon'ble jurisdictional High Court in the case of CIT v. D. G. Gopala Gowda [354 ITR 501].

06. Per contra, Ld. DR strongly supporting the order of Pr. CIT submitted that AO had never examined the issue at the time of original assessment proceedings. AO had not made any enquiries whether any interest bearing funds were utilised for giving advances to the two concerns. AO also had not examined whether any element of commercial expediency was there in such advances. Thus as per the Ld. DR, there were no enquiries made what so ever by the AO. This as per the Ld. DR rendered the order of AO erroneous and prejudicial to the interests of Revenue.

07. We have perused the orders and heard the rival contentions. What the assessee placed before the AO during the course of assessment proceedings is a break up of total other advances of Rs.4,90,22,247/- which inter alia included the sum of Rs. 4,79,69,399/- given to SRL and Rs.40,044/- given to one M/s. Stanley Properties and Hospitalities Pvt. Ltd., both of which were related parties.

08. A cursory look of Schedule IX to Balance-sheet, placed at paper book page -6, show that Rs.12,50,153/- which was the opening balance under the head "other advance", had gone up to Rs.4,90,22,294/- by the end of the year. This clearly indicate that almost whole of the loans to the sister concerns were given during the course of relevant previous year. No doubt own funds viz, share capital and reserves had gone up from Rs.10.41 crores as on 31.03.2009 to Rs.13.01 crores as on 31.03.2010. However this increase was mainly due to profit of Rs.2.60 crores of the relevant previous year. At the same time loans

raised which stood at Rs.30.04 crores as on 31.03.2009 had come down to Rs.27.33 crores as on 31.03.2010. The increase of Rs.2.6 crores in capital and reserves was not only insufficient to meet the advance of Rs.4.80 crores given to the sister concerns during the relevant previous year, but a part of it would have also gone for reducing the loans due from Rs.30.04 crores to Rs.27.33 crores. It is here that observation of the Ld. CIT that assessee had raised loan of Rs.1 crore from Engineering Design and Solutions India P. Ltd, Rs.75 lakhs from Lakshmi Narayan Vyapar and Rs.4.66 crores from Sunil Suresh, which were squared up becomes relevant. It is obvious that AO after receiving the break-up of the advances given by the assessee, never ventured to do an analysis or enquiry which a prudent man would have done on the face of the figures in P & L account and Balance-sheet filed by the assessee. Vis-a-vis the contention of the assessee that advances to sister concerns were commercially expedient, we find no such questions were asked by the AO nor any details in this regard submitted during the course of assessment proceedings. Coming to the judgment of Hon'ble Bombay High Court in the case of Reliance Utilities and Power Ltd, their Lordship had held as under at para 16 of its judgment :

16. If there be interest-free funds available to an assessee sufficient to meet its investments and at the same time the assessee had raised a loan it can be presumed that the investments were from the interest-free funds available. In our opinion, the Supreme Court in East India Pharmaceutical Works Ltd. v. CIT [1997] 224 ITR 627 had the occasion to consider the decision of the Calcutta High Court in Woolcombers of India Ltd. [1982] 134 ITR 219 where a similar issue had arisen. Before the Supreme Court it was argued that it should have been presumed that in essence and true character the taxes were paid out of the profits of the relevant year and not out of the overdraft account for the running of the business and in these

circumstances the appellant was entitled to claim the deductions. The Supreme Court noted that the argument had considerable force, but considering the fact that the contention had not been advanced earlier it did not require to be answered. It then noted that in Woolcombers of India Ltd.'s case [1982] 134 ITR 219 the Calcutta High Court had come to the conclusion that the profits were sufficient to meet the advance tax liability and the profits were deposited in the over draft account of the assessee and in such a case it should be presumed that the taxes were paid out of the profits of the year and not out of the overdraft account for the running of the business. It noted that to raise the presumption, there was sufficient material and the assessee had urged the contention before the High Court. The principle, therefore, would be that if there are funds available both interest-free and over draft 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 Commissioner of Income-tax (Appeals) and the Income-tax Appellate Tribunal.

It is clear that the presumption regarding interest-free and overdraft/ loan funds being available to the assessee was established by the assessee. Further in the said case, the profits generated during the relevant previous year was by itself sufficient to explain the source of investments as well. Observations of Hon'ble Apex Court in the case of Sun Engineering Works (P) Ltd (198 ITR 297) is also relevant. It was held that observations of court is to be understood only in the light of the questions before it and a judgment must be read as a whole. It is neither desirable nor permissible to pick out a work or sentence divorced from the context of the question and treat it as complete law.

09. As for the Hon'ble jurisdictional High Court in the case of D. G. Gopala Gowda (supra), assessee was able to establish that even if the assessment was separately made for land and building, the former as long-term capital gain and latter as short-term capital gain, still it was not liable to pay tax. It was for this

reason their Lordship held the assessment as not prejudicial to the Revenue. On the other hand in the case before us, assessee could not establish that it had interest-free funds raised during the relevant previous year to cover the investment in sister concerns. Thus both the cases relied on by the assessee are clearly distinguishable.

10. As against this what we find is that AO had made no enquiry on the aspect of investments. This by itself rendered the assessment erroneous and prejudicial to the interests of the Revenue. We uphold the finding of the CIT to this extent. However, in such circumstances the CIT should have set aside the assessment directing the AO to conduct necessary enquiries and thereafter conclude the assessment. On the other hand, CIT has directed the AO to make interest disallowance of Rs.4,01,14,554/- giving no scope for the AO make necessary enquiries. We therefore modify the order of the CIT to this extent, and direct the AO to do the fresh assessment in accordance with law. Ordered accordingly.

11. In the result, appeal of the assessee is partly allowed.

Order pronounced in the open court on 14th day of August, 2015.

Sd/-

(N. V. VASUDEVAN)
JUDICIAL MEMBER

Sd/-

(ABRAHAM P GEORGE)
ACCOUNTANT MEMBER