

THE HON'BLE SRI JUSTICE DILIP B.BHOSALE

AND

THE HON'BLE SRI JUSTICE A.RAMALINGESWARA RAO

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I.T.T.A.Nos.289 of 2003 and 6 of 2004

% 11.02.2015

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Between:

Commissioner of Income Tax-II,
Hyderabad.

.... APPELLANT

Versus

\$ Pennar Profiles Limited,
1-8-303/69/3, S.P. Road,
Secunderabad.

...RESPONDENT

< Gist:

> Head Note:

! COUNSEL FOR THE APPELLANT :- Mr.S.Vivek Chandra Sekhar

^ COUNSEL FOR RESPONDENT :- Mr. Challa Gunaranjan

? Cases Referred:

1. (1998) 233 ITR 0493
2. (2010) 231 CTR (Karnataka) 90

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THE HON'BLE SRI JUSTICE DILIP B.BHOSALE

AND

THE HON'BLE SRI JUSTICE A.RAMALINGESWARA RAO

I.T.T.A.Nos. 289 of 2003 and 6 of 2004

ORAL JUDGMENT: (per the Hon'ble Sri Justice Dilip B.Bhosale)

These appeals by the Revenue under Section 260A of the Income Tax Act, 1961 (for short 'the Act'), are preferred against the common order, dated 24.01.2003, of the Income Tax Appellate Tribunal, Hyderabad Bench 'A', passed in I.T.A.Nos.566/Hyd/98 and 439/Hyd/98. By this order, the Tribunal disposed of two appeals, one filed by the assessee and other by the Revenue, against the order, dated 14.05.1998, passed by the Commissioner of Income Tax (Appeals) (for short "CIT(A)"). The CIT (A) by that order, partly allowed the appeal filed by the assessee. The appeal before the CIT (A) was against the assessment order, dated 26.03.1997, passed by the Assessing Officer for the assessment year 1994-95 disallowing the claim of the assessee, seeking deduction of interest liability, that was converted/merged, by the financial institution, into a term loan under Section 43B of the Act.

2. The factual matrix to the extent it is relevant is that the assessee is engaged in the business of manufacturing Aluminium

Extrusions. They had filed returns of income, showing loss of Rs.3,25,34,484/-, on 29.11.1994. A notice under Section 143(2) of the Act was issued to the assessee by the Assessing Officer on 06.11.1995. After granting an opportunity of being heard to the assessee's representative, the Assessing Officer completed the assessment *vide* order, dated 26.03.1997. It has come on record that the assessee had debited the funded interest of Rs.85,42,788/- in its profit and loss account. In addition thereto, in the statement of computation of income, funded interest of Rs.1,18,16,471/-, pertaining to the assessment years 1992-93 and 1993-94 was also claimed as deduction. Thus, the assessee had debited the funded interest of Rs.2,03,59,250/- being the interest due to the financial institutions relating to the assessment years 1992-93 and 1993-94 on account of availing of loans from them. The said return was processed under Section 143(1)(a) of the Act. Ultimately, the Assessing Officer disallowed the deduction by applying the proviso to Section 43B of the Act. The assessee claimed that the interest amount payable was converted into a principal amount/term loan and, therefore, it deemed to have paid the interest as contemplated by Section 43B of the Act and therefore, entitled for deduction.

3. The only question raised and addressed, in these appeals, by learned counsel for the parties is "whether on the facts and in the circumstances of the case, the Tribunal was justified in holding that conversion of interest into a term loan can be taken as a deemed payment for the purpose of Section 43B of the Act?"

4. Mr.S.Vivek Chandra Sekhar, learned counsel appearing for the Revenue, at the outset, invited our attention to the provisions of Section 43B of the Act and contended that under any

circumstances, in view of the insertion of Explanation 3C to Section 43B, inserted by the Finance Act, 2006 with retrospective effect from 01.04.1989, unless the amount of interest has been actually paid, cannot be allowed to be deducted as claimed by the assessee. In other words, he submitted that any sum payable as interest, referred to in Clause(d) of Section 43B of the Act, which has been converted into a loan or borrowing, cannot be allowed to be deducted or deemed to have been actually paid.

5. It would be relevant to reproduce the relevant portion of Section 43B of the Act, which reads thus:

43B.Certain deductions to be only on actual payment.-

Notwithstanding anything contained in any other provision of this Act, a deduction otherwise allowable under this Act in respect of-

(a)

(b).....

(c).....

(d) any sum payable by the assessee as interest on any loan or borrowing from any public financial institution or a State Financial Corporation or a State Industrial Investment Corporation, in accordance with the terms and conditions of the agreement governing such loan or borrowing;

(e).....

(f).....

shall be allowed (irrespective of the previous year in which the liability to pay such sum was incurred by the assessee according to the method of accounting regularly employed by him) only in computing the income referred to in section 28 of that previous year in which such sum is actually paid by him:

Provided that nothing contained in this section shall apply in relation to any sum which is actually paid by the assessee on or before the due date applicable in his case for furnishing the return of income under sub-section (1) of section 139 in respect of the previous year in which the liability to pay such sum was incurred as aforesaid and the evidence of such payment is furnished by the assessee along with such return.

Explanation (1).....

Explanation (2).....

Explanation 3: For the removal of doubts it is hereby declared that where a deduction in respect of any sum referred to in

clause (c) or clause (d) of this section is allowed in computing the income referred to in Section 28 of the previous year (being a previous year relevant to the assessment year commencing on the 1st day of April, 1988, or any earlier assessment year) in which the liability to pay such sum was incurred by the assessee, the assessee shall not be entitled to any deduction under this section in respect of such sum in computing the income of the previous year in which the sum is actually paid by him.

Explanation 3A.....

Explanation 3B.....

Explanation 3C: For the removal of doubts, it is hereby declared that a deduction of any sum, being interest payable under clause (d) of this section, shall be allowed if such interest has been actually paid and any interest referred to in that clause which has been converted into a loan or borrowing shall not be deemed to have been actually paid.

Explanation 3D.....

Explanation 4.....

6. We have perused the orders passed by the authorities below and we find that the Tribunal, for dismissing the appeals filed by the assessee and the Revenue, placed reliance upon the judgment of this Court in **Commissioner of Income Tax Vs. Mahindra Nissan Allywin Limited**^[1], in short, holding that the assessee is entitled to claim deduction of the interest liability to the financial institution which had been converted into a term loan.

7. Learned counsel appearing for the assessee placed reliance upon the judgment of the Karnataka High Court in **Vinir Engineering Private Limited Vs. Deputy Commissioner of Income Tax**^[2] and submitted that similar view, as taken by this Court in **Mahindra Nissan's** case, was taken in this judgment. The Karnataka High Court having regard to the facts that fell for consideration framed the following question for consideration:

“Whether, on the facts and in the circumstances of the

case, the funded interest could be said to be non-payment of interest in the relevant year to invoke the proviso to Section 43B of the Act to disallow the deduction of interest as claimed by the appellant?

7.1 In that case, deduction sought, as claimed in the present case, by the assessee, was disallowed by the Assessing Officer, applying the proviso to Section 43B of the Act. The assessee, thereafter, had filed an application under Section 154 of the Act explaining the reasons for claiming deduction. The application was, however, rejected holding that re-schedule of interest payment by means of a fresh loan cannot be treated as interest payment deductible under Section 43B of the specific repayment schedule. The Commissioner upheld the order of the Assessing Officer. The Tribunal held that disallowance was proper and permissible under Section 143(1)(a) of the Act and dismissed the appeal. Against that order, the assessee had filed appeal under Section 260A of the Act before the Karnataka High Court, wherein, the High Court while allowing the appeal filed by the assessee in paragraph '13' observed thus:

“In view of what is stated above, we answer the substantial questions of law raised in this appeal by holding that the Tribunal was not justified in law in concluding that the funded interest could be said to be non-payment of interest in the relevant year to invoke the proviso to Section 43B of the Act to disallow the deduction of interest as claimed by the appellant. The Assessing Officer was not justified in law to make a prima facie adjustment in a proceeding under Section 143 (1)(a) of the Act by holding that there was no deemed payment of interest in the relevant year without appreciating the interest outstanding for the earlier years 1994-95 and 1995-96 had been funded by K.S.F.C. during the relevant year by a fresh loan and that the proviso to Section 43B of the Act was not applicable.” (emphasis supplied)

8. In this backdrop, we have perused the provisions contained in Section 43B of the Act, in particular, Explanation 3C thereof, which was inserted by the Finance Act, 2006 with retrospective effect from 01.04.1989. This provision was inserted in 2006 and hence, this Court in **Mahindra Nissan**'s case, had no occasion to deal with the case in the light of this provision. Insofar as the Karnataka High Court is concerned, though this provision was existing on the date of judgment, it appears that it was not brought to the notice of learned Judges and hence, the Division Bench proceeded to consider and decide the appeal of the assessee without referring to Explanation 3C appended to Section 43B of the Act.

9. As a matter of fact, from reading of Explanation 3C, in our opinion, the question as raised in the present appeals stands answered without further discussion. This provision was inserted for removal of doubts and it was declared that deduction of any sum, being interest payable under clause (d) of Section 43B of the Act, shall be allowed if such interest has been "actually paid" and any interest referred to in that clause, which has been converted into a loan or borrowing, shall not be deemed to have been "actually paid". Thus, the doubt stands removed in view of Explanation 3C. This provision was considered by the Madhya Pradesh High Court in **Eicher Motors Limited Vs. Commissioner of Income Tax**^[3] to hold that in view of the Explanation 3C appended to Section 43B with retrospective effect from 01.04.1989, conversion of interest amount into loan would not be deemed to be regarded as "actually paid" amount within the meaning of Section 43B of the Act.

10. It is not in dispute that the assessment years with which we

are concerned in the present appeals are covered by Explanation 3C, which was inserted by the Finance Act, 2006 with retrospective effect from 01.04.1989. In this view of the matter, the appeals filed by the Revenue deserve to be allowed. Accordingly, we answer the substantial question of law framed by us in favour of the Revenue and against the assessee. However, there shall be no order as to costs.

Pending miscellaneous petitions, if any, also stand disposed of.

B.BHOSALE,J

DILIP

A.RAMALINGESWARA RAO,J

Dt:11.02.2015

Note: L.R. copy to be marked: Yes/No.
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[\[1\]](#) (1998) 233 ITR 0493

[\[2\]](#) (2010) 231 CTR (Karnataka), 90

[\[3\]](#) (2009) 315 ITR 0312