

IN THE HIGH COURT OF JUDICATURE AT MADRAS

Dated: 07.11.2016

Coram:

The Hon'ble Mr.Justice NOOTY.RAMAMOHANA RAO

AND

The Hon'ble Dr.Justice ANITA SUMANTH

Tax Case Appeal No.549 of 2016

Commissioner of Income Tax,  
No.63, Race Course Road,  
Coimbatore.

.. Appellant/ Respondent

Versus

M/s. Sakthi Auto Components Limited,  
No.180, Race Course,  
Coimbatore - 641 018.  
PAN: AAEC6536J

.. Respondent / Appellant

Tax Case Appeal filed under Section 260A of the Income Tax Act, 1961 against the order of the Income Tax Appellate Tribunal, Madras 'B' Bench, Chennai, dated 04.02.2015 in ITA No.1071/Mds/2013 preferred against the order of the Commissioner of Income Tax I, Coimbatore dated 22.03.2013 F.No.120(16) 263-SACL/CIT-I:CBE/12-13 and arising out of the assessment order of the Assistant Commissioner of Income Tax, Company Circle I(1) Coimbatore order dated 27.12.2010 made in P.A.No./GIRNo.AAEC6536J in the Assessment year 2008-09.

For Appellant .. Mr.T.R.Senthilkumar,  
Standing Counsel

For Respondent .. Mr.Vijayaraghavan for  
M/s Subbaraya Aiyar

JUDGMENT

(Judgment of the Court was delivered by DR.ANITA SUMANTH., J)

1. This Tax Case Appeal at the instance of the Revenue, challenges an order of the Income Tax Appellate Tribunal, Madras, dated 04.02.2015 in ITA No.1071/Mds/2013, raising the following substantial question of law for determination:-

Whether on the facts and circumstances of the case, the Tribunal was right in holding that the interest on the amount borrowed for declaring dividend was

allowable as deduction u/s 36(1)(iii), even in the absence of profits/reserves and the treatment of such dividend as loans in the books of the assessee company?

2. A Return of Income filed by the Respondent/Assessee for Assessment Year 2008-09 was scrutinized by the Assessing Officer and an order of Assessment under Section 143 (3) of the Income Tax Act, 1961 (hereinafter referred to as 'the Act') passed on 27.12.2010. Inter alia the Assessing Officer considered the question of applicability of Section 14A of the Act to the Assessment. Thereafter, proceedings for revision under Section 263 of the Act were initiated by the Commissioner of Income Tax-I, Coimbatore, by issue of show cause notice dated 28.02.2013 on the ground that the interest payable on borrowed capital utilized for payment of dividend to the preferential shareholders was not liable to have been allowed as a deduction under Section 36(1)(iii) of the Act.

3. The Commissioner of Income Tax noted that the assessee had shown a net deficit in the profit and loss account. Thus, according to the CIT, dividend had been declared and paid from out of borrowed funds and the interest on such borrowings did not constitute allowable deduction in terms of Section 36(1)(iii) of the Act.

4. The assessee pointed out that there had been adequate cash profits on the dates of declaration of dividend and in any event, the declaration of dividend was itself for the purpose of business. Thus, according to the assessee, expenditure incurred in connection therewith constituted an allowable deduction in terms of Section 36(1)(iii) of the Act. Overruling the objections of the Assessee, an order under Section 263 of the Act came to be passed on 22.03.2013 that was challenged in appeal before the Income tax Appellate Tribunal.

5. The Tribunal, vide order dated 04.02.2015, allowed the appeal filed by the assessee after consideration of various decisions on the issue that settled the position that interest paid on borrowings for declaration of dividend constitutes expenditure incurred 'for the purpose of business' allowable as a deduction in terms of Section 36(1)(iii) of the Act. The present appeal by is filed by the Revenue assailing the aforesaid order of the Tribunal.

6. We have heard Shri T.R.Senthilkumar, learned Standing Counsel for the appellant and Shri Vijayaraghavan, learned counsel for the respondent/ assessee.

7. The learned counsel for the respondent/assessee placed before us bank statements of Axis Bank and Bank of India to the

effect that as on the dates when the dividend was, in fact declared, there was a credit balance on account of prior foreign inward remittances. Thus, and the Learned Standing Counsel does not dispute this, the assessee did have required resources internally to effect the declaration of dividend and did not have to resort to bank borrowings for the said purpose. In any event, even if borrowed funds had been utilized for the purposes of declaration of dividend, the payment of interest on such borrowings constitutes expenditure 'for the purpose of the business' of the assessee and is an allowable deduction in terms of Section 36(1)(iii) of the Act. (See CIT vs. Tingri Tea Company Ltd (79 ITR 294), Commissioner of Income Tax vs. Changdeo Sugar Mills Ltd. (1982) (31 CTR (Bom) 114, Kesar Sugar Works Ltd. vs. Commissioner of Income Tax (1997) (140 CTR 431))

8. The CIT relies on the decision of the Karnataka High Court in Kirloskar Electric Co. Ltd. vs. Commissioner of Income Tax (1997) (228 ITR 674). The Division Bench, in that case, was concerned with the allowability of expenditure incurred as dividend *per se*. The contention was that dividend paid to preference shareholders should be construed as interest paid in respect of capital borrowed 'for the purposes of business' within the meaning of section 36(1)(ii) of the Act. This was negatived by the Karnataka High Court holding that the provisions of section 36(1)(iii) cannot be stretched to include dividend in so far as preference share capital is a contribution by subscribers to the capital of a company and cannot be equated to a borrowing subject to payment of interest. Thus, expenditure incurred by way of dividend did not constitute allowable deduction in terms of section 36(1)(iii). This decision turns on different facts and does not advance the case of the revenue.

9. In the aforesaid circumstances, we do not find any merit in the appeal filed by the Revenue. The substantial question is answered against the Revenue and accordingly, the appeal stands dismissed. No costs.

Sd/-

Asst.Registrar (CO)

/true copy/

Sub Asst. Registrar

gr.

To:

1. The Registrar,  
Income Tax Appellate Tribunal,  
Madras 'B' Bench, Chennai.

2. The Commissioner of Income Tax I  
No.63 -A Race Course Coimbatore- 641 018

3. The Assistant Commissioner of Income tax  
Company Circle I(1)  
Coimbatore

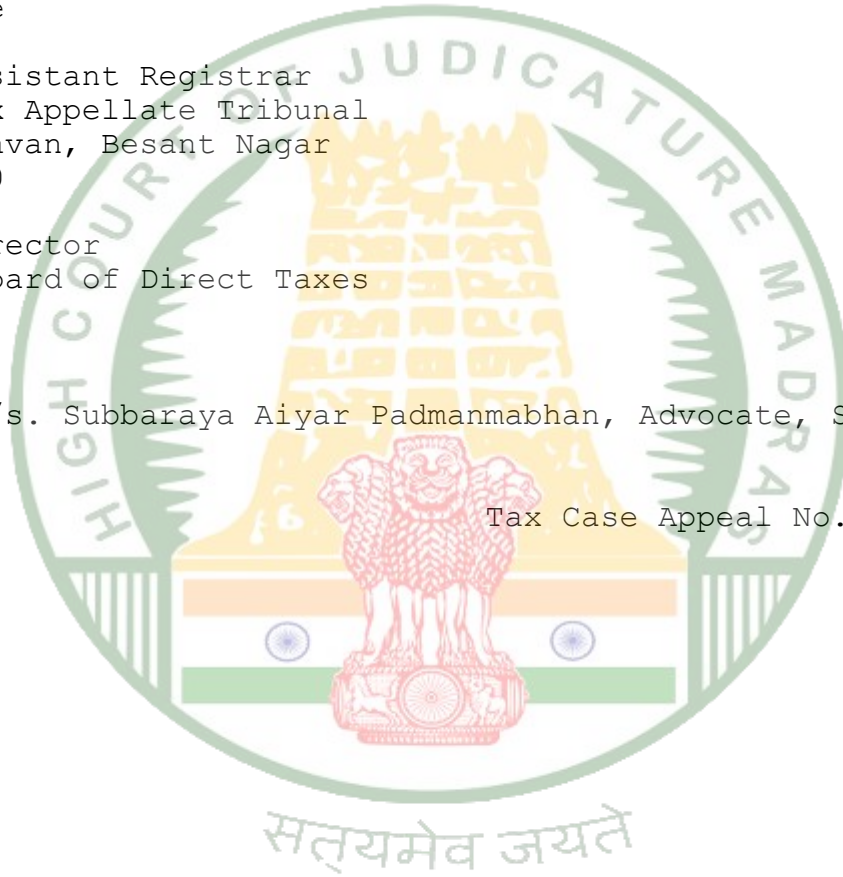
4. The Assistant Registrar  
Income Tax Appellate Tribunal  
Rajaji Bhavan, Besant Nagar  
Chennai-90

5. The Director  
Central Board of Direct Taxes  
New Delhi

1 cc to M/s. Subbaraya Aiyar Padmanmabhan, Advocate, Sr. 63763

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