IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED: 21-04-2017

RESERVED ON: 14-09-2016

CORAM:

The Hon'ble Mr.Justice NOOTY.RAMAMOHANA RAO
AND
The Hon'ble Dr.Justice P.DEVADASS

Tax Case Appeal No.415 of 2016

The Commissioner of Income tax
Chennai. ... Appellant

Versus

M/s. Alliance Infrastructure Projects
Private Limited, Bangalore.
(Cause title amended vide order
dated 9.8.2016) ... Respondent

Tax Case Appeal filed under Section 260A of the Income Tax Act, 1961, against the Order of the Income Tax Appellate Tribunal, 'C', Bench, Chennai, dated 10.04.2015 in I.T.A.No.557/Mds/2013 for the Assessment Year 2009-10, and order of the commissioner of Income Tax(APPEALS)-III Chennai-34 dated 10.12.2012 in I.T.A.No.684/11 - 12/A-III, and order of the Assistant commissioner of Income Tax company Circle 1(2), Chennai-34 dated 30.12.2011 in I.T.A.No.557/mds/2013/

For Appellant .. Mrs.Hema Muralikrishnan,
Standing Counsel
For Respondent .. Mr.N.V.Balaji.

JUDGMENT

(Judgment of the Court was delivered
by NOOTY.RAMAMOHANA RAO, J)

This Tax Case Appeal under Section 260A of the Income Tax Act, 1961 is preferred by the Revenue against the order dated 10.04.2015, rendered by the Income Tax Appellate Tribunal, Madras 'C' Bench, in I.T.A.No.557/Mds/2013, which appeal has been preferred calling in question the order of the

Commissioner of Income Tax (Appeals)-III,Chennai, dated 10.12.2012 in ITA No.684/11-12/A.III, for the Assessment year 2009-10.

2. The following substantial question of law has been framed for consideration:

> "Whether on the facts and circumstances of the case, the Tribunal was right in deleting the disallowance of Rs.21708433/- made u/s 36 (1)(iii) of the Income Tax Act? "

3. The Respondent/Assessee, a Private Limited Company is carrying on business of real estate development and construction. It had filed its Return of Income for the Assessment year 2009-10 admitting loss of Rs.34,12,997/- and offered Rs.3,77,879/- as income under Section 115JB of the Income Tax Act (in short called as the Act).

4. During the course of scrutiny of the assessment, the Assessing Officer made certain additions to the income Returned by the Assessee and in that process, disallowed interest expenditure claimed under Section 36(1)(iii) of the Act. Aggrieved by this Assessment Order dated 30.12.2011, the Assessee preferred an appeal before the Commissioner of Income Tax (Appeals). The Appellate Authority accepted the submissions of the Assessee and allowed the appeal in toto by the order dated 10.12.2012. Aggrieved by the order of the Appellate Authority, the Revenue has preferred Appeal before the Income Tax Appellate Tribunal, Madras 'C' Bench. The Tribunal has dismissed the appeal by confirming the order of the Commissioner of Income Tax (Appeals). Aggrieved by the order of the Tribunal, the Revenue is before us.

5. Heard Srimathy Hema Muralikrishnan, learned Standing Counsel for the Appellant and Sri N.V.Balaji, learned counsel for the Respondent/Assessee.

6. The whole question is confined as to whether the findings of the Commissioner of Income Tax (Appeals) in respect of disallowance under Section 36(1)(iii) of the Act is justified at all.

7. It is not in dispute that the Assessee has borrowed certain funds from bank/financing institutions for carrying on its business. It has also realized certain monies as part of its business activity. However, it has advanced a sum of Rs.49 Crores as "interest free loans" to its group companies. On the amounts borrowed by it from bank and other financing institutions, it has paid interest charges of Rs.2,86,80,198/-. This amount it has claimed as allowable expenditure. The Assessing Officer, after noticing that it has advanced monies as

interest free loans to its group companies, disallowed the interest expenditure on the ground that the Assessee has not made any attempt to reduce its debt burden.

8. Per contra, the contention of the Assessee is that it has sufficient funds of its own and therefore advanced certain monies to its group companies from out of such surplus money available with it. No part of the money which has been borrowed by it from the bank/ financing institutions has been advanced to its group companies. The monies borrowed by the Assessee from the banks and financing institutions have been faithfully spent for acquiring the title to the project site where the developmental activities are undertaken as part of its business activity. When once the Assessee has truthfully utilized the funds borrowed by it for acquiring a valid and marketable title for the land in question, which forms part of the essential ingredient of the real estate developmental activity, the very concept of diversion of funds as is allegedly attributed to it by the Assessing Officer would not arise.

9. The following are the un-controverted facts:

(i) The Assessee has availed certain financial assistance externally to the tune of Rs.20,03,78,000/- and has paid interest thereon in a sum of Rs.2,86,80,918/-.

(ii) The Assessee has utilized all of the amounts of term loan for acquiring right, title and interest over the land, forming part of the development of the project undertaken by it.

(iii) The bank/financing institution itself has disbursed directly to the Vendors Rs.17 Crores out of 20,03,78,000/- sanctioned term loan, on different dates towards purchase of the land.

(iv) Proof for this is very much available on record, as the bank itself has directly disbursed a sum of Rs.1,48,46,000/- to M/s. Soorya Developers and sum of Rs.1,06,04,000/- to M/s. Meghana Developers towards development and construction of Villas at the project site. Thus, Rs.19,54,50,000/- out of a total sum of Rs.20,03,78,000/- was disbursed by the bank/financial institution directly and hence the question of Assessee advancing any part of the borrowed monies to its group companies as interest free loan did not simply arise.

10. In the face of this fact situation, the question remains to be answered is whether the Assessee is entitled to seek allowance of the interest paid by it completely without making any effort to reduce the debt burden.

11. Learned Standing Counsel would submit that Section 36 has provided for certain deductions to be allowed in computing

the income chargeable to income tax under the head profits and gains of business as per Section 28 of the Act.

12. Section 4 of the Act enables income tax to be charged for any Assessment year in respect of total income of the previous year of every person. Under Section 2(24) income is defined to include the profits and gains. Hence Section 28 has attempted to codify what all would constitute the income arising from profits and gains of business or profession of the Assessee. Whereas Section 36 has provided for certain deductions to be allowed while computing the income arising from out of the profits and gains of the business. Clause (iii) of sub-section (1) of Section 36 has provided for the amount of the interest paid in respect of capital borrowed for the purpose of business or profession. The expressions "capital", "capital borrowed", "business" and "for the purpose of business" have got to be understood in the context of allowing the deduction in the matter of computation of income arising out of business.

13. Learned counsel for the Assessee has placed strong reliance on the judgment rendered by the Supreme Court in S.A. Builders Limited vs. Commissioner of Income Tax (Appeals) Chandigarh and Hero Cycles P.Ltd., vs. Commissioner of Income Tax, which followed the ratio in S.A. Builders Limited.

14. Per contra, learned Standing Counsel for the Revenue would submit that a three Judge Bench of the Supreme Court by the order dated 30.04.2012, while issuing notice for condonation of delay as also on the Special Leave Petitions, doubted the correctness of the ratio in S.A. Builders Limited by observing that if needs reconsideration.

15. The Supreme Court, in the case of S.A.Builders Ltd., cited supra, has laid down the test as to whether the assessee has lent money as a measure of commercial expediency, and it went on to add that the decisions relating to Section 37 of the Act would also be applicable to Section 36 (1) (iii), because, under Section 37 also, the expression used is ''for the purpose of business'' and it has been consistently held in the decisions relating to Section 37 that the expression ''for the purpose of business'' includes expenditure voluntarily incurred for commercial expediency and it is immaterial that the third party gets benefited thereby or not. In S.A.Builders Ltd.'s case, the Supreme Court has also noticed that the principle evolved by the House of Lords in Atherton v. British Insulated & Helsby Cables Ltd. (1925) 10 TC 155, has been approved and applied by the Supreme Court in Eastern Investments Limited v. CIT, (1951) 20 ITR 1 and CIT v. Chandulal Keshavlal & Co., (1960) 38 ITR 601, and, ultimately, the Supreme Court concluded that the fund advanced to a third party should be for commercial expediency,

if it is sought to be allowed under Section 36 (1) (iii) of the Act. It was also held by the Supreme Court in paragraph 34 of the said judgment that no businessman can be compelled to maximise its profits and the income tax authorities must put themselves in the shoes of the assessee and see how a prudent businessman would act. The authorities must not look at the matter from their own view point, but view it from that of a prudent businessman. The entire issue has been concluded in paragraph 35 of the said judgment as under :

> "35....However, where it is obvious that a holding company has a deep interest in its subsidiary, and hence if the holding company advances borrowed money to a subsidiary and the same is used by the subsidiary for some business purposes, the assessee would, in our opinion, ordinarily be entitled to deduction of interest on its borrowed loans."

16. The ratio in S.A.Builders Ltd.'s case has been followed by the Supreme Court later on in Hero Cycles P.Ltd v. CIT, (2015) 379 ITR 347 (SC). In fact, a Division Bench of this Court, in CIT v. Hotel Savera, reported in (1999) 102 Taxmann 247 (Madras), has noticed that the Andhra Pradesh High Court, in CIT v. Gopikrishna Muralidhar, (1963) 47 ITR 469, has held that it was not a case where any particular sum purported to be borrowed on behalf of the business was spent for household expenses but was a case where loans were taken for carrying on business of the assessee-firm, but the family used to withdraw some amounts from the business which were within the limit of capital supplied by the family. In that situation, the Court held that presumption can arise that where the assessee had both his own money as well as borrowed capital, the money lent by him came out of his own funds. This view of the Andhra Pradesh High Court was followed by the Gujarat High Court in Shree Digvijay Cement Co.Ltd v. CIT, (1982) 138 ITR 45. Hence, the Madras High Court has also subscribed to the same viewpoint.

17. In the present case, demonstrably, the moneys borrowed by the assessee from the bank have been spent exclusively towards acquiring the land together with the rights thereon, for the purpose of carrying on the primary business of the assessee. The assessee had been left with surplus sources (there is no dispute on that count) and, therefore, the moneys, which it has lent to its subsidiaries, cannot be treated to have been lent from out of funds borrowed by the assessee. We feel that the present case stands on a better footing than the earlier ones. We are in agreement with the views expressed by this Court earlier in CIT v. Hotel Savera, cited above, and we prefer to follow the ratio laid down in the decision of the Supreme Court

in S.A.Builders Ltd.'s case. However, it is true, that the Supreme Court, while entertaining a Special Leave Petition on 30.04.2012, had expressed a doubt as to the correctness of the view taken by it earlier in S.A.Builders Ltd.'s case, but, so long as the judgment in S.A.Builders Ltd. is not overruled, we cannot ignore the said principle and arrive at a different conclusion. Hence, we prefer to follow the ruling in S.A.Builders Ltd., and answer the reference in favour of the assessee and against the revenue.

18. Tax Case Appeal is dismissed accordingly. No costs.

Sd/-
Assistant Registrar

//True Copy//

Sub Assistant Registrar

gr/dixit

To
1. The Commissioner of
   Income Tax (APPEALS)-III,
   Chennai-34

2. The Assistant Commissioner of
   Income Tax Company circle 1(2),
   Chennai-34

+1cc to Mr.n.V.Balaji, Advocate, S.R.No.24401

IN T.C.A.No.415 of 2016

lrs(co)
rmp(09/05/17)