IN THE HIGH COURT OF JUDICATURE AT MADRAS
DATED : 17.12.2018

CORAM:

THE HONOURABLE MR.JUSTICE T.S.SIVAGNANAM
and
THE HONOURABLE MR.JUSTICE N.SATHISH KUMAR

Tax Case Appeal No.737 of 2017

M/s.Arun Excello Urban
Infrastructure Pvt Ltd. Bhattad Towers,
18, West Cott Road,
Chennai - 600 014. ...Appellant/Appellant

-vs-

The Deputy Commissioner of Income Tax
Company Circle 1 (1)
Chennai. .... Respondent/Respondent

Tax Case Appeal filed under Section 260-A of the Income Tax Act, 1961 against the order of the Income Tax Appellate Tribunal "C" Bench, Chennai dated 15.06.2016 in I.T.A.No.1145/MDS/2014 for the assessment year 2008-09 and against the order of the Commissioner of Income Tax(Appeals)-I, Chennai-34, and made in ITA 237/2010-11/A-1 dated 18/03/14 for the Assessment year 2008-09, and against the order of the Deputy Commissioner of Income Tax Company Circle I(1), Chennai -34 and made in PA/GIR No. AAGCA2312Q/AX-6975 dated 27/12/10 for the Assessment year 2008-09.

For Appellant : Mr.R.Sivaraman

For Respondent : Mrs.R.Hemalatha
Senior Standing Counsel

J U D G M E N T

(Judgment of the Court was delivered by
T.S.SIVAGNANAM,J.)

This appeal by the assessee, has been filed under Section 260-A of the Income Tax Act, 1961 (for brevity, the "Act"), challenging the order passed by the Income Tax Appellate Tribunal "C" Bench, Chennai, in I.T.A.No.1145/MDS/2014 dated 15.06.2016 for the assessment year 2008-09.

2. This appeal has been filed raising the following substantial questions of law:-

> "A. Whether on the facts and circumstances of the case the Appellate Tribunal was right in confirming the disallowance of interest on borrowed funds in view of Section 36(1)(iii) of the Act, when there is no direct nexus between the borrowed funds and the investment in the sister concerns, which were made only out of share capital reserves and surpluses ?
> B. Whether on facts and circumstances of the case the Appellate Tribunal was right in disallowing the entire interest paid by the Appellant, even when the loans were utilized exclusively and wholly for business purposes ?

3. Heard Mr.R.Sivaraman, learned counsel for the Appellant and Mrs.R.Hemalatha, learned Senior Standing Counsel for the Revenue.

4. The Assessing Officer while completing the assessment vide order dated 27.12.2010 held that the assessee claims entire interest paid on its borrowed capital as its expenditure. However, part of the borrowed funds has been diverted to its sister concerns. Further, the Assessing Officer held that claiming the entire interest as an expenditure incurred for the assesses's own business is not proper and a portion of the interest should be attributed to the funds diverted to the sister concerns. Further, the Assessing Officer placed reliance on the decision of the High Court of Punjab and Haryana reported in the case of Abhishek Industries Limited Vs CIT reported in 286 ITR 1. In fact, much of the observations made by the Assessing Officer stems out of the observations made in the decision in the case of Abhishek Industries (supra).

5. The assessee preferred appeal before the Commissioner of Income Tax (Appeals) - 1. The appeal was dismissed by order dated 18.03.2014. Against which, the assessee filed appeal before the Tribunal. The assessee's specific case before the first appellate authority as well as the Tribunal is as follows :-

> 2. During the same year, the appellant out of business interest, made interest free advance to its sister concerns and as on 31.03.2008, the total value of advances was as under:

Particulars	Advance (Rs.)
L&T Arun Excello realty Pvt. Ltd	2,46,00,000
Arun Excello Foundations Pvt. Ltd	4,23,21,170
Arun Fabricators	1,25,35,483
Arun Constructions	30,36,839
Total	18,24,93,492

3. The AO contended that the assessee advanced the borrowed funds to the sister concerns (without interest) and hence disallowed the entire interest on borrowed funds amounting to Rs.6177,008/- claimed u/s.36(1)(iii).

4. It is submitted that the appellant had made the above advances made to the sister concerns out of its own funds and not the borrowed funds. The appellant had total funds of Rs.53.09 crores (share capital+Reserves) on 01.04.2007). The advances to sister concerns were made out of these funds. Hence the contention of the AO is erroneous.

5. Admitting but not accepting the contention of the AO, even if the advances were made by the appellant to its sister concerns out of borrowed funds, the same were made in connection with the assessee's business and ought to he viewed in the light of commercial expediency.

6. As per Section 36(1)(iii) of the IT Act, the amount paid in respect of capital borrowed for the purpose of business or profession is an allowable expenditure.

7. Advance to L&T Arun Excello Realty Pvt. Ltd was made for the purpose of purchase of land and to meet the supply cost for constructions.

8. The advances made to Arun Excello Foundations Pvt. Ltd and Arun Fabricators were entirely to meet the expenses in the ordinary course of business.

9. In the case of Arun Constructions, there has been no outflow of funds from the appellant to Arun constructions. Arun Constructions was paid by Marg Constructions Ltd instead of paying the appellant. Hence, the appellant has debited the account of Arun constructions in its books and treated the same as advances made.

10. From the above, it is established that the appellant had lent funds to the sister

concerns with the sole motive of promoting its business interest and in aiding them to conduct the business activity hassle-free and efficiently."

6. Even before the Assessing Officer, the assessee explained that interest free loans were advanced to the sister concerns out of the share capital and reserves and surplus in possession of the assessee company. Though the Assessing Officer held that there is no direct nexus between the assessee and the sister concerns, came to the conclusion that the assessee cannot claim that the entire loans advanced to the sister concerns have been given out of its own funds and the funds in the business comes in a common kitty.

7. The Tribunal while testing the correctness of the order passed by the First Appellate Authority has not given any elaborate independent reasoning but has quoted the order passed by the CIT(A) in para 5 of the impugned order. The assessee claimed that these funds were given to the sister concerns bearing in mind the commercial expediency and relied upon the decision in the case of S.A.Builders Ltd., Vs. Commissioner of Income-Tax (Appeals) Chandigarh [288 ITR 1 (SC)]. The Tribunal would state that the return benefit is not an essential requirement and it is sufficient if the holding company (assessee) has a deep interest in its subsidiary, the assesseee should be able to prove that the assessee's subsidiary sister companies are sick or not having regular funds and are in dire need of help from the appellant company. Therefore, the Tribunal opined that for the said purpose package loans could have very well be obtained from the banks and the individuals by the sister concern instead of routing through the assessee company and dumping the interest burden on it. The Tribunal accepts that the Revenue cannot dictate as to how the business houses should function, but holds that the onus is on the assessee to explain the circumstances when the assessee wants to claim the expenditure attached to it. The Tribunal by the impugned order held that the assessee has failed to establish any commercial expediency for advancing interest-free loans to sister concerns.

8. In our considered view, the Assessing officer while stating that the assessee has diverted part of the borrowed funds to the sister concern has not given any independent reasoning on what basis the Assessing Officer was of the view that part of the borrowed funds has been diverted to its sister concerns. In fact, the Tribunal has held that the assessee company has not derived any benefit out of such advances to the sister concern. If that is so, the exercise that is required to be done is to examine whether any part of the borrowed funds was diverted to its sisters concerns. This exercise appears to have

not been done to the fullest extent. Further more, the decision in the case of Abhishek Industries (supra) is no longer good law in the light of the decision of the Hon'ble Supreme Court in Hero Cycles (P) Ltd v. Commissioner of Income-Tax (Central), Ludhiana [2015 379 ITR 347], wherein, it has been held as follows:-

> "Once it is established that there is nexus between the expenditure and the purpose of business (which need not necessarily be the business of the assessee itself), the revenue cannot justifiably claim to put itself in the arm-chair of the businessman or in the position of the Board of Directors and assume the role to decide how much is reasonable expenditure having regard to the circumstances of the case. No businessman can be compelled to maximize his profit and that the revenue 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 that of a prudent businessman."

9. The learned counsel for the assessee reiterated the submissions made by the assessee before the Tribunal and submitted that the decision of the Hon'ble Supreme Court in S.A.Builders (supra) would squarely apply to the assessee's case, wherein, the assessee had borrowed the fund from the bank and lent part of it to its sister concerns. The test in such a case was whether this was done as a measure of commercial expediency. The Hon'ble Supreme Court pointed out that the expression "commercial expediency" is an expression of wide import and includes such expenditure as a prudent businessman incurs for the purpose of business and it was further held that the expenditure may not have been incurred under any legal obligation, but yet it is allowable as a business expenditure, if it was incurred on grounds of commercial expediency.

10. In our considered view, the Tribunal has not given cogent reasons as to why the decision in the case of S.A. Builders (supra) cannot be applied to the facts of the present case.

11. The learned counsel for the appellant placed reliance on the decision of the High Court of Bombay in the case of Commissioner of Income-tax Vs. Reliance Utilities & Power Ltd, [2009 313 ITR 340 (Bombay)], wherein, it has been held that if there are funds available both, interest-free and overdraft and/or loans are 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 are sufficient to meet the investments.

12. Thus, considering the facts and circumstances of the case, we deem it appropriate that the Assessing Officer has to take a fresh look into the matter, as we are not satisfied on the basis on which the Assessing Officer had come to the conclusion that part of the borrowed funds have been diverted by the assessee to its sister concerns. Thus, we are inclined to remand the matter for fresh consideration. One more reason which convinced us that the Assessing Officer should take a fresh look is that the judgment in Abhishek Industries (supra) has been held to be no longer good law in the light of the decision of the Hon'ble Supreme Court in Hero Cycles (supra). This aspect also has to be noted by the Assessing Officer while re-doing the assessment.

13. For the above reasons, the appeal filed by the assessee is allowed and the orders passed by the Tribunal, the CIT (A) as well as the assessment order are set aside and the matter is remanded to the Assessing Officer to take a fresh decision in the assessee's case bearing in mind the observations made in this judgment. The substantial questions of law are left open. No costs.

Sd/-
Assistant Registrar(CS VI)

//True Copy//

Sub Assistant Registrar

svki

To

1.The Deputy Commissioner of Income Tax
Company Circle 1 (1)
Chennai - 600 034.

2.The Income Tax Appellate Tribunal "C" Bench, Chennai

+1cc to Mr.T.Ravikumar, Advocate, S.R.No.87631
+1cc to Mr.R.Sivaraman, Advocate, S.R.No.88538

TCA.No.737 of 2017

VGII(CO)

rrs 05/02/2019