

IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED :: 21-02-2019

CORAM

THE HON'BLE DR.JUSTICE VINEET KOTHARI

AND

THE HON'BLE MR.JUSTICE C.V.KARTHIKEYAN

T.C.A.No.166 of 2019

The Commissioner of Income Tax,
Chennai. Appellant

-vs-

M/s.Shriram Investments ... Respondent
Mookambika Complex
No.4 Lady Desika Road
Mylapore, Chennai-600 004.

Appeal under Section 260A of the Income Tax Act, 1961, against the order of the Income Tax Appellate Tribunal, Chennai 'B' Bench, dated 19.07.2018, passed in ITA No.995/CHNY/2017, against the order dated 30/01/2017 made in ITA No.207/CIT(A)-2/2015-16 passed by the Commissioner of Income Tax (Appeals)-2, Chennai-34 and against the order dated 05/01/2016 passed by the Deputy Commissioner of Income Tax, Non-Corporate Office-2, Chennai for the assessment year 2012-13.

For Appellant : Mr.T.Ravikumar,
Senior Standing Counsel.

For Respondent : Mr.R.Sivaraman

JUDGMENT

(Judgment of the Court was delivered by Dr.Vineet Kothari, J.)

Revenue has filed this Appeal under Section 260-A of the Income Tax Act, in short, 'Act', aggrieved by the order passed by the learned Income Tax Appellate Tribunal, in short, 'Tribunal', Chennai 'B' Bench, dated 19.07.2018, passed in ITA No.995/CHNY/2017, allowing the Assessee's Appeal for Assessment Year 2013-2014, and setting aside the addition of alleged excessive interest paid by the Assessee, an Investment Company, to its Group Companies under Section 36 (1) (iii) of the Act.

2. The following Substantial Question of Law is proposed for consideration by this Court :

"Whether on the facts and circumstances of the case, the Tribunal was right in deleting the disallowances made under Section 36 (1) (iii) of the Income Tax Act, 1961, especially when the Assessee had advanced interest bearing fund without charging any interest to its associate concerns ?

3. Mr. T. Ravikumar, learned Senior Standing Counsel for the Revenue, urged before us that the Assessing Authority as well as the Commissioner of Income Tax (Appeals) had rightly disallowed the claim of interest by the Assessee under Section 36 (1) of the Act, but the Tribunal has erred in deleting the said addition, as the Assessee had also borrowed sums from its Group Concerns and on the basis of 'Matching Principles', since lesser interest paid to the Group Concerns, it was contrary to the Agreement Clause (10) of one of the Deeds of Partnership, from whom such finance was taken, which provided for interest rate up to 12% per annum and, accordingly, the difference of interest paid and received by the Assessee should be added back under Section 36 (1) (iii) of the Act.

4. The learned Senior Standing Counsel, however, submitted that for the previous Assessment Years 1992-1993 and 1994-1995, similar appeal filed by the Revenue has been dismissed by a Co-ordinate Bench of this Court on 17.09.2014 in the case of CIT v. Shriram Investments (Firm), Moogambika Complex, Chennai, (2015) 54 Taxmann.com 15 (Madras), but the findings of the learned Tribunal in this regard in the present case are not justified. He also submitted that the decision of the Hon'ble Supreme Court in the case of S.A. Builders Ltd. v. Commissioner of Income Tax (Appeals), (2007) 288 ITR 1 (SC), in this regard, has been referred to a Larger Bench of the Hon'ble Supreme Court at a later stage in the case of Additional Commissioner of Income Tax v. Tulip Star Hotels Ltd. in an S.L.P. in C.C.Nos.7138-7140 of 2012, by an order dated 30.04.2012.

5. On the other hand, learned counsel for the Assessee submitted that applying of 'Matching Principles' by the Assessing Authority as well as CIT (A) in the present case was incorrect and not sustainable, as the Assessee company, being an Investment Company, had applied cash basis of accounting and the actual amount of interest paid and received was recorded by it. He reiterated the findings of the learned Tribunal in Para 7 in this regard and the same are quoted below for ready reference :

"7. We have considered the rival contentions

and perused the orders of the authorities below. Assessee had debited in its profit and loss account, only the actual interest paid and credited only the actual interest received, since it was following the cash system of accounting. In our opinion in a cash basis of accounting system, there is no question of applying any matching principle. Interest is credited as income at point of receipt and debited as expenses at the point of payment. According to the disparity in the period for which interest is received and paid, there could be difference. That apart, copy of the partners current account placed at paper book page 10, shows that debit balances in partners current account arose more on account of losses suffered in the earlier years, than due to any drawings by the partners. It might be true that it had received interest only from four individuals to which it had advanced amounts during the relevant previous year. This does not mean that assessee had not received interest from other parties in other years. During the previous assessment year 2009-2010, it had received interest of Rs.13,34,06,510/- from persons to whom it had advanced loans. Hence in our opinion, it is obvious that disparity between interest received and interest payment arose not on account of any selective charging of interest, but on account of cash basis system followed by the assessee. There is nothing in the statute which stopped the assessee from following the cash system of accounting. In assessee's own case for assessment year 2009-2010 on Revenue appeal (ITA No.1690/Mds/2013, dated 27.11.2013), this Tribunal had held as under :-

'6. The Commissioner of Income Tax (Appeals) held that the assessee is an investment company made investments in group concerns as part of its business of the assessee i.e. advancing loans to group concerns. The Commissioner of Income Tax (Appeals) also gave a finding that monies are borrowed from group concerns only and these monies are utilized by the investee concerns for their trade purposes. Since the investments in shares of group concerns amounting to Rs.4,38,00.000/- are within the course of trading activities

and out of commercial expediency and the decision of the Hon'ble Hon'ble Supreme Court in the case of S.A.Builders (288 ITR 1) is applicable to the assessee. The Commissioner of Income Tax (Appeals) also held that Rs.76,58,00,000/- invested in sister concerns as share application money is not capable of yielding any income nor any right to a benefit is vested in, therefore provisions of Section 14A are not attracted in view of the decision of the Co-ordinate Bench of this Tribunal in the cases of MSA Security Services and NMS Consultancy P. Ltd (supra). The Department could not rebut any of the findings of the Commissioner of Income Tax (Appeals). Therefore, we sustain the order of the Commissioner of Income Tax (Appeals) in deleting the disallowance made under Section 14A of the Act. The grounds raised by the Revenue are rejected'.

Thus assessee has been considered as an investment company and making investments was part of its business. Hon'ble Jurisdictional High Court also in the case of CIT vs. Shriram Investments (Firm), (2015) 54 taxmann.com 15 also held that deduction u/s.36(1) (iii) of the Act had to be allowed in respect of interest paid, if capital was borrowed for the purpose of business or profession. As already mentioned by us, there is no finding by any of the lower authorities that disparity between interest receipts and payments arose on account of charging of lower rate of interest on loans advanced when compared to interest paid on loans received. In the circumstances, we are of the opinion that Id. Assessing Officer was not justified in making a disallowance for the difference between interest received and interest paid by the assessee. Disallowance of Rs.1,65,81,384/- stands deleted."

6. We have heard the learned counsel for the parties and also gone through the order impugned of the learned Tribunal.

7. A Co-ordinate Bench of this Court, in the case of Assessee itself, for the previous Assessment Years in T.C.A.No.2657 of 2006 and other connected matters, decided on 17.09.2014, had held in favour of the Assessee that deduction under Section 36 (1) (iii) of the Act was allowed, though the Assessee had borrowed the capital for the purpose of business of

investments. The relevant portion of the said judgment is also quoted below for ready reference :

"7. We may firstly consider the first three questions as to whether the interest of borrowed capital which was utilised in the business of shares both by way of investment and stock-in-trade is allowable deduction.

In so far as first three questions are concerned, in our opinion, a co-ordinate Bench of this court in CIT v. Lokhandwala Construction Inds.Ltd. (2003) 260 ITR 579 (Bom.), had addressed itself to this issue. Reliance was placed on India Cements Ltd. v. CIT (1966) 60 ITR 52 (SC) which was under Section 10 (2) (iii) of the Income-Tax Act, 1922 which corresponds to Section 36 (1) (iii) of the present Act. This Court answered the issue in the following manner (page 581) :

'That, while adjudicating the claim for deduction under section 36 (1) (iii) of the Act, the nature of the expense-whether the expense was on capital account or revenue account- was irrelevant as the section itself says that interest paid by the assessee on the capital borrowed by the assessee was an item of deduction. That the utilization of capital was irrelevant for the purpose of adjudicating the claim for deduction under section 36 (1) (iii) of the Act. (see the judgment of the Bombay High Court in the case of Calico Dyeing & Printing Works v. CIT (1958) 34 ITR 265. In that judgment, it has been laid down that where an assessee claims deduction of interest paid on capital borrowed, all that the assessee had to show was that the capital which was borrowed was used for business purpose in the relevant year of account and it did not matter whether the capital was borrowed in order to acquire a revenue asset or a capital asset.'

It may be noted that in India Cements Ltd. v. CIT (1966) 60 ITR 52 (SC), the apex court was specifically pleased to observe that the object of the loan is an irrelevant consideration. In the State of Madras v. G.J.Coelho (1964) 53 ITR 186 (SC) , the Supreme Court was dealing with the deduction claimed under section 5 (e) of the

Madras Plantations Agricultural Income-tax Act, 1955. While considering the issue, the court was pleased to observe that in principle there is no distinction between interest paid on capital borrowed for the acquisition of a plantation and interest paid on capital borrowed for the purpose of an existing plantation. Both are for the purpose of the plantation. The court further observed that the payment of interest on the amount borrowed for the purpose of the plantations when the whole transaction of purchase and the working of the plantations was viewed as an integrated whole was so closely related to the plantations that the expenditure could be said to be laid out or expended wholly and exclusively for the purpose of the plantations.

8. We may also gainfully refer to the judgment of the Calcutta High Court in CIT v. Rajeeva Lochan Kanoria (1994) 208 ITR 616. The learned court was considering section 36 (1) (iii) and was pleased to observe as under (page 620) :

I 'The only enquiry that is to be made is whether the payment of interest was in respect of capital borrowed for the purpose of the assessee's business or profession. There is no dispute that the capital was borrowed in the instant case and interest was paid on the borrowed capital. It is to be established that the amount was borrowed for the purpose of business or profession. The amount borrowed may be utilized for the purpose of acquisition of stock-in-trade or for the purpose of acquisition of capital assets. But so long as the money is utilised for business purposes the interest will have to be allowed as deduction. It is well settled that business expenditure is not confirmed to expenses incurred on revenue account. Capital expenditure may not be allowed as a deduction under section 37 because the section specifically bars any deduction of expenditure of capital nature. But section 36 is differently worded. There is no bar in section 36 (1) (iii) to allowance of interest paid in respect of capital borrowed which has been utilised

for purchase of a capital asset. The position of law in this regard was explained by the Supreme Court in the cases of India Cements Ltd. v. CIT (1966) 60 ITR 52 (SC) and State of Madras v. G.J.Coelho (1964) 53 ITR 186 (SC)'' (emphasis supplied).

8. We have considered the reasoning given in the decisions referred to supra and are in respectful agreement with the view expressed in the said decisions, for the reason already given by us that there is nothing in Section 36 (1) (iii) of the Act that would dis-entitle the assessee to claim deduction in respect of interest paid on the capital borrowed for the purposes of business.

9. For the foregoing reasons, we uphold the concurrent findings rendered by the Commissioner of Income Tax (Appeals) and the Tribunal and answer substantial question of law against the Revenue and in favour of the assessee. These appeals are dismissed. No costs."

8. The Hon'ble Supreme Court, in the case of S.A.Builders, cited supra, held that it will depend upon the facts and circumstances of the respective case and unless the money advanced to a sister concern cannot be held to have been advanced for commercial expediency of the assessee, the interest paid thereon by the borrower Assessee cannot be disallowed under Section 36 (1) (iii) of the Act. Para 36 of the said judgment is quoted below for ready reference :

"36. We wish to make it clear that it is not our opinion that in every case interest on borrowed loan has to be allowed if the assessee advances it to a sister concern. It all depends on the facts and circumstances of the respective case. For instance, if the Directors of the sister concern utilize the amount advanced to it by the assessee for their personal benefit, obviously it cannot be said that such money was advanced as a measure of commercial expediency. However, money can be said to be advanced to a sister concern for commercial expediency in many other circumstances (which need not be enumerated here). 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."

9. We are of the considered opinion, that, as a matter of fact, no substantial question of law arises in the present case, because, it is essentially a finding of fact as to whether the lower interest paid on the borrowings made by the assessee company from the sister concerns or the group companies is for the purpose of its business or not. Whether it is commercially expedient or not for the Assessee cannot be decided by the Revenue authorities and unless a decision taken in the usual course of business by the Assessee can be held to be arbitrary or motivated, deliberately taken to defeat the purpose of the Revenue, it cannot be held that the lower interest rate paid to the borrowers on the borrowings made by the assessee company is disallowable under Section 36 (1) (iii) of the Act. No such finding of fact has been recorded by the Tribunal. On the contrary, in Para 7 of the Tribunal's order, quoted above, the Tribunal, in our opinion, rightly held that when the cash system of accounting was adopted by the Assessee, an Investment Company, whose business is only to borrow and lend or invest, the same cannot be said to be not in the business interest or commercially expedient for the purpose of business and the concept of 'Matching Principles', which has been applied by the Assessing Authority and the CIT (A) in the present case, was not really applicable. It is not for the Revenue authorities to substitute their own wisdom or notion about the rate of interest agreed to between the parties, including the group companies and, as such, the finding of fact about commercial expediency or absence thereof is a finding of fact, out of which, no substantial question of law can be said to be arising, requiring our consideration under Section 260A of the Act. Moreover, since in the case of Assessee company itself, this Court has only decided on similar facts earlier and dismissed the Revenue's Appeal, we do not find any reason to take a different view of the matter for the Assessment Years in question before us.

10. Therefore, this Appeal, filed by the Revenue, is also liable to be dismissed and it is, accordingly, dismissed. No costs.

Sd/-
Assistant Registrar (CS-IV)

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Sub Assistant Registrar

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To

1. Income Tax Appellate Tribunal, Chennai 'B' Bench, Chennai.
2. The Commissioner of Income Tax (Appeals)-2, Chennai-34
3. The Deputy Commissioner of Income Tax, Non-corporate Office-2, Chennai.

T.C.A.No.166 OF 2019

SAI (CO)
GMY (03/04/2019)



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