GAURI AMIT GAEKWAD
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IN THE HIGH COURT OF JUDICATURE AT BOMBAY
ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO.1911 OF 2017

The Pr. Commissioner of Income Tax - 3 ….Appellant

V/s.

V. Hotels Limited ….Respondent

Mr. Suresh Kumar for appellant.
Mr. P.J. Pardiwalla, Senior Advocate i/b. Mr. Atul K. Jasani for respondent.

CORAM : K.R. SHRIRAM &
AMIT B. BORKAR, JJ.
DATED : 22nd NOVEMBER 2021

P.C. :

1 In this appeal, the following two substantial questions of law have been proposed :

> *(a) Whether on the facts and in the circumstances of the case, the Hon'ble ITAT was justified in allowing depreciation on intangible assets amounting to Rs.1,54,43,383/- as claimed by the assessee when the said disallowance of depreciation made by the Assessing Officer had been confirmed by the CIT(A) in view of the fact that the hotel operation of the appellant was suspended during the year under consideration as per the Auditors Report?*

> *(b) Whether on the facts and in the circumstances of the case and in law, the Hon'ble ITAT was justified in deleting the disallowance of interest claim of 9% amounting to Rs.1,60,22,465/- in respect of the fully convertible debentures issued to M/s. Cox and Kings India Ltd. without appreciating the fact that Shri Ajay Ajit Peter Kerkar, who is the son of Shri Ajit B. Kerkar, Chairman of the assessee company, was the Director of M/s. Cox and Kings India Ltd. during the relevant period and therefore, the provisions of Section 40A(2) are applicable and also the comment of the Auditors in the Audit Report that the interest claimed by the assessee company in respect of interest paid @ 24% is prejudicial to the interest of the company and the AO has reasonably made the disallowance of the excess claim of interest of 9%?*

2 With reference to question no.1, Mr. Suresh Kumar states that it is squarely covered by an order passed by this Court on 17th December 2018 in Income Tax Appeal No.835 of 2016 with Income Tax Appeal No.836 of 2016.

3 As regards the second question, in our view, it does not raise any substantial question of law in as much as, the entire basis of the Assessing Officer's opinion is based on the noting made by the auditors in the annual report of respondent that payment of interest at 24% on Fully Convertible Debentures (FCD's) was prejudicial to the interest of the company.

4 According to the Assessing Officer, one Mr. Ajay Ajit Peter Kerkar, the son of Mr. Ajit B. Kerkar, Chairman of respondent, happens to be a Director of Cox and Kings India Ltd. and working for the said company from 1986. Though he has not said so in so many words, from the question proposed and the findings of the ITAT, it does appear that the Assessing Officer was relying upon sub Section 2 of Section 40A of the Income Tax Act, 1961 (the said Act). Even for a moment we proceed on the basis that Cox and Kings India Ltd. would come under the definition of person stated in clause (b) of sub Section 2 of Section 40A, the Assessing Officer has to form an opinion that the expenditure was excessive or unreasonable having regard to the fair market value of the goods, services or facilities for which the payment is made or the legitimate needs of the business or profession of

respondent or the benefit derived by or accruing to him therefrom.

5 In this case, respondent had issued debentures to Cox and Kings India Ltd. amounting to Rs.18 Crores during the Assessment Year 2005-2006 for a period of 89 days. Due to ongoing litigation, respondent's hotel was not functional and respondent had huge financial liabilities. In view of this, respondent was unable to redeem the debentures and requested Cox and Kings India Ltd. to roll over the debentures. Cox and Kings India Ltd. agreed but with a condition - enhancing the rate of interest on these debentures. Respondent agreed to pay interest at 24% p.a. on the debentures. Indisputably, Cox and Kings India Ltd. has disclosed and offered to tax 24% p.a. that they received on the debentures subscribed to by them.

6 In the assessment year, if one considers the assessment order, the Assessing Officer has not placed any material under identical facts and circumstances to justify that the fair market rate of interest was lower than what respondent has paid. The Assessing Officer has not recorded any finding or collected any material to show that the interest paid by respondent was in excess of the fair market rate. Section 40A (2) (a) reads as under :

> *40A (2) (a) Where the assessee incurs any expenditure in respect of which payment has been or is to be made to any person referred to in clause (b) of this sub-section, and the Assessing Officer is of opinion that such expenditure is excessive or unreasonable having regard to the fair market value of the goods, services or facilities for which the payment is made or the legitimate needs of the business or profession of the assessee or the benefit derived by or*

> *accruing to him therefrom, so much of the expenditure as is so considered by him to be excessive or unreasonable shall not be allowed as a deduction:*
>
> *Provided that for an assessment year commencing on or before the 1st day of April, 2016 no disallowance, on account of any expenditure being excessive or unreasonable having regard to the fair market value, shall be made in respect of a specified domestic transaction referred to in Section 92BA, if such transaction is at arm's length price as defined in clause (ii) of Section 92F.*

As provided under Section 40A (2) (a), the Assessing Officer was duty bound to form a personal opinion, after having regard to the fair market value of the goods, services or facilities for which payment is made, that such expenditure is excessive or unreasonable. As stated earlier, there is no material placed to indicate what would have been the fair market value of interest that would have been payable on the debentures and why such payment was excessive or unreasonable. Simply relying on the auditors' finding is not enough.

7 Moreover, the ITAT has rightly concluded that the provisions like Section 40A are meant to check evasion of tax through excessive or unreasonable payment to relatives and associate concerns and should not be applied in a manner which will cause hardship in bonafide cases relying on Section 40A(2) of the Act. Moreover, it is not a case of tax evasion in as much as it is not the Revenue's case if the rate would have been less the assessee's profit would have been more. As could be seen from the assessment order itself respondent had filed return of income for Assessment Year 2010-2011, which is the year in question, declaring loss at

Rs.31,88,44,909/- and the return of income had been processed under Section 143 (1) of the Act. We find support for this view from the judgment of the Division Bench of this Court (Panaji Bench) in ***Commissioner of Income Tax V/s. V.S. Dempo and Co. P. Ltd.***[1].

8 In our view, the Tribunal has not committed any perversity or applied incorrect principles to the given facts and when the facts and circumstances are properly analysed and correct test is applied to decide the issue at hand, then, we do not think that question as pressed raises any substantial question of law.

9 The appeal is devoid of merits and it is dismissed with no order as to costs.

(AMIT B. BORKAR, J.) **(K.R. SHRIRAM, J.)**

1. 2011 (336) ITR 209 (Bom.)