

**IN THE INCOME TAX APPELLATE TRIBUNAL
(DELHI BENCH 'B' : NEW DELHI)**

**BEFORE SHRI A.T. VARKEY, JUDICIAL MEMBER
and
SHRI PRASHANT MAHARISHI, ACCOUNTANT MEMBER**

**ITA No.4768/Del./2012
(ASSESSMENT YEAR : 2007-08)**

ITO, Ward 11 (2),
New Delhi.

vs.

M/s. First American Securities Pvt. Ltd.,
C/o Luthra & Luthra Law Offices,
103 – A, Ashoka Estate,
Barakhamba Road,
New Delhi – 110 001.

(PAN : AAACF2072N)

(APPELLANT)

(RESPONDENT)

ASSESSEE BY : Shri Sumit Mangal, CA &
Ms. Varsha Bhattacharya, Advocate
REVENUE BY : Shri Hemant Gupta, Senior DR

ORDER

PER A.T. VARKEY, JUDICIAL MEMBER :

This appeal, at the instance of the revenue, is filed against the order of the Commissioner of Income-tax (Appeals)-XIII, New Delhi dated 18.06.2012 for the assessment year 2007-08.

2. The revenue has taken the following grounds of appeal :-

“1. The Learned CIT (A) has erred on the facts and circumstances of the case and in law in deleting the addition of Rs.1,64,53,604/- on account of interest paid on capital expenses i.e. loan taken for investment in shares of jointly controlled entity for purpose of substantial control over the entity to acquire management control over the organization. This is transaction on

capital account and enduring nature. The same cannot be held revenue expenses.

2. The Learned CIT(A) has erred on the facts and circumstances of the case and in law for allowing the expenses when assessee has not carried out any business activity during the year except for parking of its investible fund in equity shares of a closely associated concern.

3. The appellant craves leave to add, alter or amend any ground of appeal raised above at the time of hearing.”

3. The assessee company is a joint venture entity between the AXA India Holdings and Bharati Enterprises (Holdings) P. Ltd and was engaged in the business of investments. The return of income was filed by the assessee on 31.10.2007 declaring loss of Rs.1,18,34,157/-. The case was processed u/s 143(1) of the Income-tax Act, 1961. Subsequently, the case was selected for scrutiny and notice u/s 143(2) of the Act was issued on 24.09.2008. During the year under consideration, the assessee company declared NIL gross receipts and posted a net loss of Rs.2.20 crores which after necessary adjustments in computation of income was reduced to a loss of Rs.1.18 crores. During the course of assessment proceedings, the assessee had debited an amount of Rs.1,64,53,604/- under the head "Interest on unsecured loans". The assessee raised capital and unsecured loans during the year under consideration and invested the same in long term unquoted equity shares of M/s Bharati Axe Life Insurance Co. Ltd of Rs.57.80 crores. The AO asked the assessee to show cause as to why the interest expenses not be deemed to be capital in nature being related to long term investment in unquoted shares of a jointly controlled entity. However, the AO observed that no specific reply was furnished by the assessee.

It was further observed that the assessee had made the investment in the shares of a jointly controlled entity for the purpose of substantial control over such entity and the shares were not tradable freely being unquoted and the investments were also classified as long term. In view of the nature of the investment, the AO observed that the apparent purpose of strategic control and close nexus between the assessee and the investee concern, it could be safely concluded that it was not a trade investment for business purposes. The AO further observed that by mere description of its business as that of making strategic investments, the assessee could not camouflage the real nature of the transaction which was to acquire management control over the organization, which was a transaction on the capital account. Accordingly, the AO held that the interest expenses of Rs.1,64,53,604/- are capital in nature and could not be claimed as revenue expenditure. Further, the AO observed that the assessee has not carried out any business activity during the year except for parking of its investible funds in equity shares of a closely associated concern. In view of this, the AO held that the only expense which would be allowable would be that which was incurred by the assessee mandatorily to survive as a corporate concern, i.e., the Audit fee of Rs 28,090/-. Accordingly, the AO completed the assessment u/s 143 (3) of the Act.

4. The assessee filed an appeal before the first appellate authority and the Id. CIT (A) while allowing the appeal of the assessee held the interest expenses of Rs.1,64,53,604/- as revenue expenditure as under :-

“6.3 Decision

I have considered the submission of the appellant and observation of the Assessing Officer. It is seen that appellant company is a joint venture entity between AXA India Holdings and Bharti Enterprises (Holdings) Pvt. Ltd. The business of the appellant company is to make strategic investments in the business entities. During the F.Y. 2006-07 the appellant company has invested a sum of Rs.57,80,03,400/- for subscribing the equity shares of Bharti AXA Life. This fact is duly reported in the Audited Financial Statement of the appellant company for F.Y. 2006-07 at schedule-S in the balance sheet. From this activity of the appellant company, it is established that it has commenced its business activities and has made investments during the period, therefore, the findings of the Assessing Officer that appellant company has not commenced its business activities is not based on proper appreciation of facts.

As regards the Assessing Officer's decision of treating the interest payment claimed of Rs.1,13,15,271/- as capital expenditure. It is seen that provisions of section 36 (1)(iii) of the IT Act are very clear in this regard and the same are reproduced hereunder :-

"36(1) The deduction provided for in the following clauses shall be allowed in respect of the matters dealt with therein in computing the income referred to in section 28 -

(iii) the amount of the interest paid in respect of capital borrowed for the purposes of the business or profession :

[Provided that any amount of the interest paid in respect of capital borrowed for acquisition of an asset for extension of existing business or profession (whether capitalised in the books of account or not): for any period beginning from the date on which the capital was borrowed for acquisition of the asset till the date on which such asset was first put to use, shall not be allowed as deduction.]"

It is seen that the amount of interest claimed by the appellant is in respect of capital borrowed for the purpose of business or profession carried out by the appellant company during the year. The capital borrowed has not been utilized for acquisition of any asset or for extension of any business or profession, therefore, the interest paid on the capital borrowed for business purposes has to be an allowable business expenditure. The same cannot be denied. It is very specifically mentioned in the objects of the MOU that appellant company is to make strategic investment in the business entities. In follow up that object during the F.Y. 2006-07 it has made strategic investment of Rs.57,80,03,400/- in Bharti AXA Insurance Co. Ltd. Therefore, the interest expenditure incurred by the appellant company is for business purposes of the appellant company. This fact has been acknowledged by the Assessing Officer himself in the assessment order wherein he has stated that appellant has "*parked its investible funds in the equity shares of a closely associated concern*". Hence, there was no basis for treating the interest expenditure

claimed by the appellant as capital expenditure, Therefore, the expenditure claimed by the appellant on account of interest is an allowable revenue expenditure and disallowance made by the Assessing Officer is deleted.

Reliance in this regard is placed on following judicial pronouncements:-

Commissioner of Income-tax, Panaji Goa v. Phil Corpn. Ltd. [2011] 14 taxmann.com 58 (Bom.)

Section 36(1)(iii) of the Income-tax Act, 1961. Interest on borrowed capital - Assessee took loan from overdraft account and invested it into sister/subsidiary concern and claimed deduction under section 36(1)(iii) in respect of interest payable to bank which was disallowed by Revenue authorities. Tribunal found that overdraft was not used for mere investment in shares of sister subsidiary company to earn dividend but was used to have control over that company and further that such an investment was integral part of business of assessee. Whether assessee was entitled to deduction of interest paid on overdraft under section 36(1)(iii) - Held yes [In favour of assessee]

FACTS

The assessee took a loan of Rs.3,70,00,000 from the bank and invested the same into its sister concern P, though no dividend was received by the assessee. The assessee claimed a deduction under section 36(1)(iii) in respect of the interest payable by it to the bank. The Assessing Officer held that since the investment was out of borrowed funds for business, the proportionate interest was to be disallowed. He further observed that since the assessee was entitled to receive an amount or 20 per cent from P on account of I.C.D. an amount of Rs.19,73,333 was to be disallowed and was, therefore, added to the gross total income. The Commissioner (Appeals) confirmed the order of the Assessing Officer. The Tribunal, however, found that the assessee had invested the amount in question in subsidiary company P for the acquisition of its shares, i.e. to have a control over majority shares but not to earn dividend. It was clear that such an investment was integral part of the business. Therefore, the Tribunal came to the conclusion that the assessee was entitled to the amount as deduction under section 36(1)(iii).

On appeal by the revenue :

HELD

The reasoning of the Tribunal that the overdraft was not operated only for investing in the shares of subsidiary company and the fact that it was also used for investment in the shares of the sister/ subsidiary company to have control over that company and, therefore, the element of interest paid on the overdraft was not susceptible of bifurcation and, therefore, the assessee was entitled to the deduction under section 36(1)(iii). [Para 11]

Thus, the Tribunal was right in deleting the addition of Rs.19,73,333. [Para 12]”

SRISHTI SECURITIES (P.) LTD. V. JOINT COMMISSIONER OF INCOME-TAX, SPL. RANGE 39 [2005] 148 TAXMAN 49 (MUM.) (MAG.)

I. Section 36(1)(iii) of the Income-tax Act, 1961 - Interest on borrowed capital - Assessment year 1997-98 - Whether if funds are borrowed by an investment company for making investment in shares which may be held as investment or as stock-in-trade or for purpose of controlling interest in other companies, interest paid on such borrowed funds will be deductible under section 36(1)(iii) - Held, yes

II. Section 28(i) of the Income-tax Act, 1961 - Business loss/deductions - Allowable as - Assessment year 1997-98 - Assessee claimed loss on account of valuation of stock of certain shares valued at cost or market price whichever was lower - Assessing Officer rejected valuation on ground that shares were held as investment and not as stock-in-trade - Assessee contended that shares were acquired for investment originally and were later converted into stock-in-trade - Whether since revenue authorities had not properly examined issue, same was to be restored back to Assessing Officer - Held, yes

Facts-I

The assessee an investment company utilized borrowed funds for acquiring shares by way of investment as well as by way of stock-in-trade. It also acquired certain shares in various companies with a view to acquire controlling rights in certain companies. On the borrowed funds, the assessee paid interest and claimed deduction of same under section 36(1)(iii). The Assessing Officer disallowed the entire interest on the ground that the primary object or acquiring the shares was not to earn dividend but to acquire controlling interest in companies. On appeal, the Commissioner (Appeals) held that to the extent, the borrowed funds were used for acquiring shares by way of stock-in-trade, the assessee was entitled to deduction for interest and on that basis, he allowed interest to that extent.

On appeal:

Held-I

In the case of CIT v. Lokhandwala Construction Industries Ltd. [2003] 260 ITR 579 (Bom.), it was held that interest paid on capital borrowed for business purpose is allowable irrespective of the fact as to whether the capital was borrowed to acquire a revenue asset or a capital asset. Therefore, if funds are borrowed by an investment company for making investment in shares which may be held as investment or as stock-in-trade or for the purpose of controlling interest in other companies, interest paid on such borrowed funds will be deductible under section 36(1)(iii).

Therefore, interest expenditure was allowable under section 36(1)(iii) and the disallowance to the extent sustained by the Commissioner (Appeals) was directed to be deleted.

Facts-II

The assessee claimed loss on account of valuation of the stock of certain shares by valuing them at cost or market price whichever was lower. The Assessing Officer rejected the valuation on the ground that the said shares were held as investment and not as stock-in-trade. On appeal, the Commissioner (Appeals) confirmed the order of the Assessing Officer. In the appeal, the assessee contended that the shares were acquired for investment originally and were later converted into stock-in-trade.

Held-II

The revenue authorities had not properly examined the issue. Therefore, the issue was restored back to the Assessing Officer with the direction that the assessee's claim that investments were converted into stock-in-trade with reference to the entries made in the books of account of the relevant year in which the alleged conversion took place might be verified.

In the result, for statistical purposes, the assessee's appeal was to be allowed.”

The facts of the above cited judicial pronouncements are identical with the facts of the appellant's case, therefore, the ratio of the said judgment is squarely applicable with to the appellant's case. Therefore, the Assessing Officer was not justified in treating the interest payment on loan taken for business purposes as capital expenditure. Hence, the same is deleted.”

5. Being aggrieved, the revenue is in appeal before us.
6. The ld. DR relied on the order of the AO. He submitted that in view of the nature of the investment, the apparent purpose of strategic control and close nexus between the assessee and the investee concern, it can be safely concluded that it is not a trade investment for business purpose. He further submitted that by mere description of its business as that of making strategic investments, the assessee cannot conceal the real nature of the transaction which is to acquire management control over the organization, which is a transaction on capital

account. He, therefore, submitted that the AO has rightly held these interest expenses of Rs. 1,64,53,604/- as capital in nature. He further submitted that during the year, assessee has not carried out any business activity except for parking of its investible funds in equity shares of a closely associated concern. He submitted that the Ld.CIT (A) has wrongly concluded that mere investing in its own concern without having any return during the year is business activity of the company during the year. Therefore, it is not justified in treating the interest payment on loan taken for the purpose to park in own concern as business activity and treating it to be revenue expenditure. He submitted that since business of the assessee has not commenced during the year, therefore, AO has rightly disallowed all the expenses except mandatory one and Ld. CIT (A) has wrongly deleted all the disallowances made by AO. He, therefore, prayed that the order of the Id. CIT (A) be set aside and that of the AO be restored.

7. On the other hand, the Id. AR, while reiterating the submissions made before the Id. CIT (A), submitted that the tax deductibility of interest paid on capital borrowed for the purposes of business is covered u/s 36(1)(iii) of the Act. The Id. AR, in order to explain the ambit and scope of the applicability of section 36(1)(iii), relied on the case of CIT vs. Dalmia Cement (P.) Ltd. – 254 ITR 377 (Del.). Further, the Id. AR relied on the decision of Tetron Commercial Ltd. Vs. CIT – 261 ITR 422 (Cal.) wherein the Hon'ble Calcutta High Court has elaborately explained the scope of deductibility of expenses u/s

36(1)(iii). Ld. AR submitted that on the basis of the above precedents, it becomes abundantly clear that even if capital borrowed by the taxpayer is utilized on the capital account, the interest paid by the taxpayer on such borrowed capital would be allowable as deduction u/s 36(1)(iii) of the Act as long as the said capital expenditure is incurred for the purpose of business. He submitted that the very business of the assessee is that of making strategic investments for which the assessee has borrowed money and paid interest thereon. Thus, there can be no doubt that the expense incurred by the assessee by way of payment of interest on such unsecured loan is a business expenditure and allowable as deduction u/s 36(1)(iii) of the Act. The Id. AR, in order to substantiate its claim, further relied on the decision of CIT vs. Phil Corporation Limited – (2014) 14 Taxmann.Com 58 (Bom.) wherein the Hon’ble Court has held as under :-

“We find that the reasoning of the ITAT that the overdraft was not operated only for investing in the shares of subsidiary company and the fact that it was also used for investment in the shares of the subsidiary company to have control over that company and, therefore, the element of interest paid on the overdraft was not susceptible of bifurcation and therefore, the respondent no.1 is entitled to the deduction under Section 36(1)(iii) of the Income-tax Act is correct and deserves to be accepted.”

He further relied on the decision of Srishti Securities (P.) Ltd. vs. JCIT – 2005-(148)-Taxman-0049-TBOM. Ld. AR submitted that on the basis of above judicial pronouncements, it can be safely concluded that interest paid by an investing company, on the funds used for making investment in other entities with the objection of acquiring / maintaining controlling interest in such entities,

is a deductible expense u/s 36(1)(iii) of the Act. He submitted that in the present case, the assessee is a joint venture entity between AXA and Bharti formed with the business objection of making strategic investment in Bharti AXA Life, therefore, the business of the assessee is to invest in Bharti AXA Life. In this view of the matter, Id. AR submitted that the Id. CIT (A) rightly held the expenses as revenue in nature and prayed to uphold the order of the Id. CIT (A).

8. We have heard both the parties and perused the material on record. The main controversy in this case is whether the expenditure claimed by the assessee on account of interest is capital expenditure or revenue expenditure. We are in agreement with the Id. CIT (A) that the expenditure is to be treated as revenue in nature because the assessee is an investment company. We take note that assessee-company is a joint venture entity between AXA India Holdings and Bharti Enterprises (Holdings) Pvt. Ltd. and the business of the assessee company is to make strategic investments in the business entities. We find that during the year under consideration, the assessee has invested a sum of Rs.57,80,03,400/- for subscribing the equity shares of Bharti AXA Life and this fact was duly reported in the Audited Financial Statement of the assessee company at Schedule-S in the balance sheet. By doing this activity, it has commenced its business activities and has made investments during the period, therefore, the findings of the Assessing Officer that assessee has not commenced its business activities is erroneous and not based on proper

appreciation of facts as held by Id. CIT (A). We further find that the amount of interest claimed by the assessee is in respect of capital borrowed for the purpose of business or profession carried out by the assessee company during the year, therefore, the interest paid on the capital borrowed for business purposes has to be an allowable business expenditure and the same cannot be denied. We also find that it is very specifically mentioned in the objects of the MOU that assessee company is to make strategic investment in the business entities and accordingly, it has made strategic investment of Rs.57,80,03,400/- in Bharti AXA Insurance Co. Ltd. Therefore, we find that the interest expenditure incurred by the assessee is for business purposes. And also, this fact is acknowledged by the AO himself in the assessment order wherein he has stated that assessee has *"parked its investible funds in the equity shares of a closely associated concern"*. Hence, we find that there was no basis for treating the interest expenditure claimed by the assessee as capital expenditure.

8.1 Our above view is also fortified by the decision of Commissioner of Income-tax, Panaji Goa v. Phil Corpn. Ltd. [2011] 14 taxmann.com 58 (Bom.) wherein the Hon'ble High Court held that, *"The reasoning of the Tribunal that the overdraft was not operated only for investing in the shares of subsidiary company and the fact that it was also used for investment in the shares of the sister/ subsidiary company to have control over that company and, therefore, the element of interest paid on the overdraft was not susceptible of bifurcation and, therefore, the assessee was entitled to the deduction under section*

36(1)(iii).” Further, the ITAT, Mumbai Bench in the case of Srishti Securities (P.) Ltd. vs. JCIT (supra) held that if funds are borrowed by an investment company for making investment in shares which may be held as investment or as stock-in-trade or for purpose of controlling interest in other companies, interest paid on such borrowed funds will be deductible under section 36(1)(iii).

8.2 In view of the above, we are of the opinion that the ratio of the aforesaid judgments is squarely applicable to the assessee’s case and the Id. CIT (A) has rightly held that the expenditure as revenue in nature in the facts of the case. Accordingly, we do not find any infirmity in the order of the Id. CIT (A) and uphold the same. The grounds raised by Revenue are rejected.

9. In the result, the appeal of the revenue is dismissed.

Order pronounced in open court on this day of 11th January, 2016.

**Sd/-
(PRASHANT MAHARISHI)
ACCOUNTANT MEMBER**

**sd/-
(A.T. VARKEY)
JUDICIAL MEMBER**

**Dated the 11th day of January, 2016
TS**

Copy forwarded to:

- 1.Appellant
- 2.Respondent
- 3.CIT
- 4.CIT(A)-XIII, New Delhi.
- 5.CIT(ITAT), New Delhi.

**AR, ITAT
NEW DELHI.**