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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

\+ **INCOME TAX APPEAL No. 205/2018**

Date of decision: 28th September, 2018

PRINCIPAL COMMISSIONER OF INCOME TAX-7..... Appellant

Through: Mr. Asheesh Jain, Sr. Standing Counsel with Mr. Shahrukh Ejaz, Advocate for Income Tax Department.

versus

THE BASTI SUGAR MILLS COMPANY LIMITED..... Respondent

Through: Mr. Piyush Kaushik, Advocate.

CORAM:
HON'BLE MR. JUSTICE SANJIV KHANNA
HON'BLE MR. JUSTICE CHANDER SHEKHAR

SANJIV KHANNA, J. (ORAL):

This appeal by the Revenue under Section 260A of the Income Tax Act, 1961 ['Act' for short], in the case of The Basti Sugar Mills Company Limited, ['respondent-assessee' for short] relates to the Assessment year 1999-2000 and arises from the order of the Income Tax Appellate Tribunal ['Tribunal'] dated 18th August, 2017.

2. This is second round of litigation. By the order dated 24th November, 2010 passed by the Delhi High Court in ITA No. 1248/2007 the issue of disallowance of Rs. 1,50,04,133/- under Section 36(1)(iii) of the Act was

remitted to the file of the Assessing Officer in light of the judgment of the Supreme Court in ***S.A. Builders LTD versus Commissioner of Income Tax***, (2007) 1 SCC 781.

3. The Assessment Order on remand observes that the respondent-assessee had been asked to adduce material to prove that the interest free advances to sister concerns were out of its own funds and not out of borrowed capital from the bank on which there was interest liability. This was necessary to examine the question of "commercial expediency". The respondent-assessee having expressed their disability to correlate each and every entry of the advances to the sister concerns with availability of its own funds, there was failure to justify and explain commercial expediency in giving interest free advances of Rs.8,33,56,295/- to the sister concerns. Accordingly, the ratio in ***S.A. Builders*** (Supra) would not apply.

4. Clearly, the Assessing Officer had attempted to ascertain the source of funds of the amounts given as interest free loans to the sister concerns, in order to examine and apply the test of "commercial expediency". Unable to ascertain the details from the respondent-assessee, it was held that the test of commercial expediency was not satisfied. We would observe that the Assessing Officer had posed a wrong question and, therefore, his reasoning is infelicitous and contrary to law. ***S.A. Builders*** (Supra) does not require the respondent-assessee to show that the borrowed funds had not been used for giving interest free advances or loans to the third party, including sister concerns. The issue “commercial expediency” is different. The Supreme Court in ***S.A. Builders*** (Supra) had observed that Section 36(1)(iii) of the Act states that interest paid in respect of capital borrowed for the purpose of

business or profession is to be allowed as a deduction in computing taxable income. The expression "for purposes of business or profession" occurring in Section 36(1)(iii) of the Act is wider in scope than the expression "for the purpose of earning income, profits or gains". Accordingly, expenditure voluntarily incurred on the test of commercial expediency is to be allowed as a deduction. It is immaterial if a third party also benefits by the said expenditure. The expression "commercial expediency" is again of wide import and includes such expenditure incurred for the purpose of business. Therefore, once it is established that there was a nexus between expenditure and purpose of business, which need not be the business of the assessee, deduction under Section 36(1)(iii) of the Act must be allowed. Revenue cannot assume the role and occupy armchair of a businessman to decide whether expenditure was reasonable. The Revenue cannot look at the matter from its own standpoint, but that of a businessman. Money borrowed, even when advanced to a sister concern for some business purpose, would qualify for deduction of interest. However, if the money borrowed is utilized by the assessee for personal benefit and not for business purpose, interest paid on that amount would not satisfy the test of commercial expediency.

5. There is another glaring error by the Assessing Officer. Instead of disallowing interest paid on the borrowed fund, the Assessing Officer made an addition of Rs. 1,50,04,133/- by notionally computing interest @18% p.a. on Rs.8,33,56,295/- i.e. the interest free advances given by the respondent-assessee to the sister concerns. This is clearly impermissible and contrary to law.

6. The Commissioner of Income Tax (Appeals) referring to the 'nexus principle' approved in ***S.A. Builders*** (Supra) held that once link between the expenditure given by way of loans and the purpose of the business was established, Revenue cannot justifiably assume the role of the assessee to decide how much was reasonable expenditure having regard to the circumstances of the case. The test of "commercial expediency" would only come into play if there was any finding that interest bearing funds had been diverted for making interest free loans. Interest free loans were given prior to 1st April, 1998 as per the schedule of secured loans and unsecured loans in the balance sheet as on 31st March, 1998. The loans taken by the respondent-assessee were for specific purposes and were duly represented by the value of stock. He observed that the respondent-assessee during the period relating to the Assessment Year had sales of Rs.37.16 crores, paid up share capital of Rs.8.20 crores and reserves of Rs.1.23 crores. He concluded that the respondent-assessee had furnished ample evidence to show that sufficient funds were available to give interest free loans. Accordingly, addition of Rs. 1,50,04,133/- was directed to be deleted. The aforesaid factual reasoning negates and nullifies the factual reasoning given by the Assessing Officer.

7. Agreeing with the said factual finding and not finding any justification to upset the facts as found by the first appellate authority, the Tribunal has dismissed the appeal filed by the Revenue.

8. Decision of the Supreme court in ***S.A. Builders***(supra) has been followed in ***Hero Cycles Private Limited versus Commissioner of Income Tax*** (2015) 16 SCC 359 and ***Munjal Sales Corporation versus Commissioner of Income Tax and Another*** (2008) 3 SCC 185. The reasons

and grounds given in the assessment order cannot be supported and sustained in view of the ratio of the said decisions.

9. Recording the aforesaid, we do not find any merit in this appeal and the same is dismissed, with no order as to costs.

SANJIV KHANNA, J.

CHANDER SHEKHAR, J.

SEPTEMBER 28, 2018
MR