

आयकर अपीलीय अधिकरण, 'बी' न्यायपीठ, चेन्नई
IN THE INCOME TAX APPELLATE TRIBUNAL, 'B' BENCH, CHENNAI
श्री एन.आर.एस. गणेशन, न्यायिक सदस्य एवं श्री ए. मोहन अलंकामणी, लेखा सदस्य केसमक्ष
BEFORE SHRI N.R.S.GANESAN, JUDICIAL MEMBER
AND SHRI A.MOHAN ALANKAMONY, ACCOUNTANT MEMBER

आयकर अपील सं./I.T.A.No.1649/Mds/2015

(निर्धारण वर्ष / Assessment Year: 2012-13)

The Deputy Commissioner of Income Tax, Corporate Circle-I(2), Chennai-34.	Vs	M/s. Chennai Network Infrastructure Pvt.Ltd., 34/1, New No.403L, 7 th floor Samson Tech Park, Pantheon Road, Egmore, Chennai-600 006.
		PAN: AADCC8088Q
(अपीलार्थी/Appellant)		(प्रत्यर्थी/Respondent)

अपीलार्थी की ओर से/ Appellant by	:	Mr. P.Radhakrishnan, Advocate
प्रत्यर्थी की ओर से/Respondent by	:	Mr. V.Manish Shah

सुनवाई की तारीख/Date of hearing	:	20 th June, 2016
घोषणा की तारीख /Date of Pronouncement	:	9 th September, 2016

आदेश / ORDER

Per A. Mohan Alankamony, AM:-

This appeal is filed by the Revenue aggrieved by the order of the learned Commissioner of Income Tax (Appeals)-1, Chennai dated 30.03.2015 in ITA No.59/CIT (A)-12013-14 passed under section 143(3) r.w.s 250(6) of the Act.

2. The Revenue has raised several grounds in its appeal, however, the cruxes of the issues are as follows:-

"i) The learned Commissioner of Income Tax (Appeals) has erred in holding that the

assessee is entitled to claim deduction under section 57(iii) of the Act towards the proportional interest expenditure incurred on the borrowings from bank against the interest income earned from banks on the term deposits(sourced from such bank loan) kept during the preoperative period.

ii) The learned Commissioner of Income Tax (Appeals) has erred in holding that the assessee is entitled to set off the interest income earned on ICD from the pre-operative expenditure claimed by the assessee since the interest earned from advancing the share application money towards ICD's do not fall under the category of borrowed funds and do not involve any payment of interest and is inextricably linked with the business of the assessee.

iii) The learned Commissioner of Income Tax (Appeals) has erred in directing the learned Assessing Officer to verify the claim of the assessee regarding the investment made in "growth mutual funds" amounting to ₹1,67,51,972/- which was disallowed by the learned Assessing Officer by invoking the provisions of section 14A of the Act.

3. Brief facts of the case are that the assessee is a subsidiary company of M/s. GTL Infrastructure Ltd., engaged in the business of providing sharable passive infrastructure facilities to various telecom/mobile operators filed its return of income for the assessment year 2010-11 on 22.07.2011 admitting income of ₹49,06,271/-. The case was selected for

scrutiny and notice under section 143(2) was issued to the assessee. Subsequently, the assessment was completed by the learned Assessing Officer under section 143(3) of the Act on 14.03.2013 wherein he made addition of Rs.18,17,00,903/- under the head 'income from other source' and disallowed the expenditure of Rs.1,67,51,972/- as deduction invoking the provisions of section 14A of the Act. On appeal, the learned Commissioner of Income Tax (Appeals) deleted the disallowance of Rs.18,17,00,903/- and remitted back the issue with respect to disallowance made by invoking the provisions of section 14A of the Act.

Ground No.1 & 2: Deduction u/s.57(iii) of the Act and set off of interest income earned on ICD's from pre-operative expenditure :-

4.1. The above mentioned issues are concised by the learned Commissioner of Income Tax (Appeals) in his order is as follows:-

"During the year, the assessee availed unsecured loans for a total sum of Rs.4500,02,64,937/- and made investments in fixed deposits of Rs.155,00,00,000 as well as advanced loan as inter-corporate deposit of Rs.2987,85,00,000. The appellant has

received a total interest of Rs. 18,17,00,902/- from the deposits made. The appellant has adjusted the said interest income against the preoperative expenses pending capitalization amounting to Rs. 63,99,68,349/-. The AO proceeded to tax the aforesaid interest income on the temporary deployment of the loan funds as income from other sources. The interest expenditure claimed against the interest income was disallowed by AO and added to the cost of acquisition of capital asset. Reliance was placed on the decision of Supreme Court in the case of Chellapalli Sugars Ltd and Tuticorin Alkali Chemicals & Fertilizers Ltd, (227 ITR 172) wherein interest income earned at preoperative stage is held to be taxed under Income from other sources. Further reliance was also placed on the decision of jurisdictional High Court of Madras in the case of Seshasayee Paper & Boards Ltd reported in 156 ITR 542 (1985).

4.2 The learned Authorized Representative had made the following submissions before the learned Commissioner of Income Tax (Appeals):-

“(i) The case of the appellant is squarely covered by the decision of the Delhi High Court in Indian Oil Panipat Power Consortium Ltd v. ITA (315 ITR 255) and NTPC Sail Power Company P. Ltd v. CIT (ITA No. 1238/Del/2011) wherein identical facts of the Hon'ble High Court has held that the pre-operative interest earned from temporary deployment of funds should be reduced from the project cost and not considered as income chargeable to tax under Sec. 56 of the Act.

(ii) It is evident from the assessment order that the above legal principles and findings have not been denied/negated/disputed in the assessment order, however, the only reason for denying the claim of the appellant on the alleged ground that the facts of the aforesaid cases before the Hon'ble Delhi High Court are different from the appellant's own case and therefore, the claim of the appellant has been rejected.

(iii) Further, similar view has been taken by the Hon'ble Punjab and Haryana High Court in the case of CIT v. Arihant Threads Ltd (12 Taxmann.com 69) holding that the matter is covered in favour of the assessee by judgments of the Hon'ble Supreme Court in Kamal Cooperative Sugar Mills Ltd's case (243 ITR 2)

and Bokaro Steel Ltd case.

(iv) Without prejudice to the above,

(a) The appellant submit that the Id. AO erred in not allowing expenses u/s.57 of the Act against the interest income treated as the income from other sources.

(b) The pre-operative expenses incurred by the appellant consists of the upfront fees, interest on borrowed funds, miscellaneous expenses etc. that ought to be allowed while calculating the income chargeable under the head "Income from Other Sources" u/s.57 of the Act.

(c) In the event, it is held that the interest income is revenue receipt that applying the matching principle the expenses incurred for earning the alleged income should be allowed as a deduction in computing such income u/s. 57 of the Act.

(d) In this regard, reliance is placed on the following decisions:

(i) CIT vs. VGR Foundations (298 ITR 132)

(ii) CIT vs. Sasan Power Ltd (18 Taxmann.com, 182)

(iii) DCIT v. Jhagadia Cooper Ltd (ITA No. 1191/AhdI2008)

The appellant humbly submits that if the interest is treated as income from other sources, then the expenses incurred to earn such interest income ought to be allowed as deduction u/s. 57 of the Act. "

4.3 Thus, the issue before the learned Commissioner of Income Tax (Appeals) was twofold concised herein below:-

i) Whether the assessee would be entitled to claim deduction under section 57(iii) towards the proportional interest expenditure against the interest income of Rs.4.61 crores received from term deposits of Rs.1555 crores kept in fixed deposits with the bank which was sourced from the loan of Rs.4500.96 crores obtained from the bank.

ii) Whether the assessee would be allowed to set off interest received amounting to Rs.13.5 crores on ICDs from the pre-operative expenses wherein the source of the ICDs were from the interest free share application money of Rs.3559.24 crores received by the assessee.

4.4 On the first issue, the learned Commissioner of Income Tax (Appeals) by relying in the decision of the jurisdictional High Court in the case CIT Vs. VGR Foundation reported in 298 ITR 132 held that the interest earned during pre-operative period has to be set off under section 57(iii) of the Act in the case of the assessee. The gist of his finding is extracted herein below for reference:

"4.2.3 With regard to interest received from the banks on term deposits of Rs.4.61 crores, no doubt the amount needs to be taken as income from other sources by following the decision of the Hon'ble Supreme Court in the case of Tuticorin Alkali (supra). When it is taken as revenue receipt by following the above decision the next issue is whether expenses incidental to it should be allowed to be set off u/s 57(iii) of the Act. The provisions speak as under-

Deductions.

57. The income chargeable under the head "Income from other sources" shall be computed after making the following deductions, namely:-

- (i) ...
- (ii) ...
- (iii) any other expenditure (not being in the nature of capital expenditure) laid out or expended wholly and exclusively for the purpose²⁹ of making or earning such income;

As seen from the above, the expenditure which is wholly and exclusively related for the purpose of earning income is only allowed to be claimed and set off against such income. In the instant case, the appellant has borrowed money from the banks to run the business but not to give the amount for earning 'interest, therefore, in my considered opinion the stipulation of the above provisions are not fulfilled to claim a set off. However, the Id.AR has put forth his arguments in his written submissions stating that the deduction u/s 57(iii) needs to be allowed to be claimed from the interest income received from the term deposits. In support of his claim he has relied on the following decisions -

- (i) Rajendra Prasad Moody (115 ITR 519) (SC)
- (ii) Steeleo Gujarat Ltd (99 ITD 408) (IT AT Ahmedabad)
- (iii) Jhagadia Copper Ltd (ITA NO.3253/Ahd/2008 and 3545/Ahd/2008)

In all these cases, especially in the first case, it was held that the claim of s.57(iii) should be taken independently and if such expenditure is otherwise a proper expenditure should not be denied to be claimed just because there was no receipt of income. It says "Whatever is a proper outgoing by way of expenditure must be debited irrespective whether there is receipt of income or not." The Courts have felt that the provisions of s.56 & 57 are independent and the expenditure enumerated u/s 57 cannot be denied to be claimed just

because there was no income u/s 56. In other words, the expenditure enumerated u/s 57 needs to be allowed to be set off against such income u/s 56 if the said expenditure is genuine and proper. Even though the scales of these judgments tilt in favour of the appellant, the facts and circumstance of the appellant case is different and these judgments are not applicable in the instant case. These are the judgments which have nothing to do with income generated and expenditure incurred at a preoperative stage whereas the case on hand is related to a situation where the income earned and expenditure incurred was related to a preoperative stage where the expenditure needs to be capitalized. However, in the case of VGR. Foundations (298 ITR 132) (Mad.), the jurisdictional High Court has given the decision in favour of the assessee and this is a case where the facts and circumstances are similar to that of the appellant i.e., the earning of income and incurring of expenditure are related to preoperative stage. The question raised by the Revenue before the High Court against the order of the ITAT Chennai Bench is as under-

"Whether, on the facts and in the circumstances of the case, the Income-tax Appellate Tribunal was right in holding that interest on moneys borrowed for the period prior to the commencement of business can be allowed as deduction from the interest under section 57 of the Act while computing 'Income from other sources' in respect of the interest received?

The jurisdictional High Court has answered the above question positively and in favour of the assessee by stating as under-

"Under the circumstances, we do not find any error or legal infirmity in

the order of the Tribunal so as to warrant interference. Hence, no substantial question of law arises for consideration of this court and accordingly the tax cases are dismissed. Consequently, M.P.No.1 of 2007 in TC. (A) NO.610 of 2007 is closed. No costs."

Thus, going by the decision of VGR Foundations (supra), the interest earned during preoperative period has to be set off u/s 57(iii) of the Act.

4.4.1 From the facts of the case it is evident that out of the bank loan of Rs.4500.96 crores the unutilized portion of Rs.1,555 crores was placed in fixed deposit with the bank by the assessee. Therefore, the source of the FD is directly linked to the bank loan obtained by the assessee wherein there is a cost, being the proportional interest payable to the bank. Section 57(iii) of the Act makes it amply clear that any expenditure incurred for the purpose of earning income which is taxable under the head "Income from other source" has to be allowed as deduction. In the above case, for the interest income earned by the assessee there is a direct link to the proportional interest paid by the assessee. Therefore, as per section 57(iii) of the Act, the assessee would be entitled to the benefit of deduction with respect to the proportional

interest expenditure incurred by the assessee towards earning interest income. Moreover, as pointed out by the assessee the Hon'ble Apex Court in the case Bokaro Steels Ltd., reported in 236 ITR 325 has relaxed the decision rendered in the case of Tuticorin Alkalis Chemicals & Fertilizers reported in 227 ITR 172 by holding that interest income earned during pre-operative period should go to reduce the expenditure if it is inextricably linked with the setting up of the capital structure of the assessee company. Hence, the decision of the Hon'ble Apex Court in Tuticorin Alkalis Chemicals & Fertilizers will not be squarely applicable to the case of the assessee. Likewise the learned Commissioner of Income Tax (Appeals) has relied in the decision of the Hon'ble jurisdictional High Court in the case of VGR Foundation cited supra, wherein facts are identical and held the issue in favour of the assessee. Therefore, we do not find it necessary to interfere with the order of the Ld.CIT(A) on this issue.

4.4.2 On the second issue also the learned Commissioner of Income Tax (Appeals) following the

decision of the Hon'ble jurisdictional High Court in the case of VGR Foundation cited supra has held that the assessee is entitled to set off the interest income earned on ICDs from the pre-operative expenditure because the share application money received by the assessee company do not fall under the category of borrowed fund and is inextricably linked with the business of the assessee. The gist of the relevant portion of the learned Commissioner of Income Tax (Appeals) is reproduced herein below for reference:-

"4.2.4 With regard to denial of set off of interest on ICDs from the preoperative expenditure also, the jurisdictional High Court decision in the case of VGR Foundations (supra) relied on by the appellant clearly covers wherein the decision goes in favour of the appellant. The jurisdictional High Court has confirmed the order of the ITAT, Chennai which has given its ruling in assessee's favour by following its own earlier order. The relevant paras of the jurisdictional High Court are produced as under-

"Learned standing counsel appearing for the Revenue submitted that the assessee had set off interest earned, prior to the commencement of the business operation, against the expenses. The assessee is wrong in setting off the interest prior to the commencement of the business operation against the expenses. The interest income earned prior to the commencement of the business has to be assessed under the head "Income from other sources". Hence, the Assessing Officer is right in assessing the interest income under the head "Income from other sources". Heard counsel. The Tribunal allowed the appeals by following its own earlier order and accepted the contention of the assessee. The Tribunal, in its order, held as follows:

"5. Before me learned counsel for the assessee also relied on the decision of the Supreme Court in the case of CITv. Karnataka Power Corporation [2001] 247 ITR 268, wherein it was held that interest receipts / hire charges received during pre-production is on capital account. Learned counsel for the assessee also relied on various decisions in support of his case. At the time of hearing he had also filed a copy of the order of this Tribunal in I.T.A. No. 1369/Mds/02, dated November 11, 2002, wherein on identical issue the Tribunal considering the various Supreme Court decisions observed and held as under:

'4. The Supreme Court in Tuticorin Alkali Chemicals and Fertilizers Ltd. [1997] 227 ITR 172 was considering investment of borrowed funds prior to commencement of business and held that the interest earned was taxable. In Bokaro Steel Ltd. [1999] 236 ITR 315, it was a case of a Government company which during the period of construction of the plant had advanced monies to contractors on which it was earning interest, received rent from quarters let out to employees, received hire charges on plant let out to contractors and received royalty on stones removed from the assessee's lands. The Supreme Court considered all these activities to be intricately connected with the construction activity and accordingly held that interest received, rent received, hire charges and royalty, etc., would be reduced from the cost of the assets and it would not be treated as income. Similar view was expressed by the Supreme Court in the case Kamal Co-operative Sugar Mills Ltd. [2000] 243 ITR 2. Identical view was also taken by the Supreme Court in the cases of Bongaigaon Refinery and Petrochemicals Ltd. [2001] 251 ITR 329 and Karnataka Power Corporation [2001] 247 ITR 268.

5. In our opinion, in view of the above clear cut ruling by the Supreme Court it is necessary to give a finding of fact in regard to monies that were kept in deposit from out of the share application monies. In the light of the Supreme Court decision in Tuticorin Alkali Chemicals and

Fertilizers Ltd. [1997] 227 ITR 172, it is only in the event of interest earned from out of deposits made from borrowed funds that it would be in the nature of income. Share application monies do not fall into the category of borrowed funds and do not involve payment of interest. In effect share application monies, etc., are gathered for being used in setting up of an industry, unit, purchase of assets, and so on. Till such time the money is required for deferment of various items, obviously the money has to be kept in deposit with a bank. Keeping the money in current account would not yield any interest income. It can, therefore, be seen that it is during the course of construction that the monies are kept in deposits with the bank. In these circumstances in the light of the Supreme Court decisions in the cases of Bokaro Steel Ltd. [1999] 236 ITR 315, Kamal Co-operative Sugar Mills Ltd. [2000] 243 ITR 2 and Karnataka Power Corporation [2001] 247 ITR 268, the claim of the assessee is reasonable and deserves to be accepted. We accordingly uphold the claim of the assessee and delete the addition of interest made to the income. The legal plea was not insisted upon."

From a reading of the above, it is seen that the Tribunal has followed the principles enunciated in the Supreme Court judgments in the case of CIT v. Bokaro Steel Ltd. [1999] 236 ITR 315 and in the case of Karnataka Power Corporation [2001] 247 ITR 268, and came to the correct conclusion. The Revenue is unable to give any further materials or evidence and also not able to furnish information as to whether they have filed any appeal against their earlier order or not.

Under the circumstances, we do not find any error or legal infirmity in the order of the Tribunal so as to warrant interference. Hence, no substantial question of law arises for consideration of this court and accordingly the tax cases are dismissed. Consequently, M.P. NO.1 of 2007 in T.C. (A) No. 610 of 2007 is closed. No costs."

4.2.5 In view of the above discussion, it is clear that the appellant is entitled to claim deduction u/s 57(iii) from the interest income earned from the banks on term deposits kept

with them during preoperative period. Similarly, the appellant is entitled to set off the interest income earned on ICDs from the preoperative expenditure claimed by the appellant since the interest earned from depositing the share application moneys as ICDs do not fall under the category of borrowed funds .and do not involve payment of interest and are inextricably linked with the business of the appellant. In the result, the disallowance made by the AO is directed to be withdrawn. The ground is allowed.”

4.4.3 From the above decisions of the Hon’ble jurisdictional High Court, in the case of VGR Foundations and the decision of the Hon’ble Apex Court in the case of CIT Vs. Bokaro Steels Ltd., supra, and the decision of the Tribunal(supra), it is evident that the interest received from ICDs the source of which are from share application money which is interest free has to be set off against the pre-operative expenses of the assessee because they are inextricably linked to the setting up of the business of the assessee. Since the learned Commissioner of Income Tax (Appeals) has only followed the decision of the above mentioned higher judiciaries while arriving at his decision and given relief to the assessee, following the same ratio, we do not find it necessary to interfere with his order on this issue.

5. Accordingly, both the grounds 1 & 2 are decided in favour of the assessee and against the Revenue.

Ground No.3: Disallowance of Rs.1,66,51,972/- under section 14A of the Act:

6. The learned Assessing Officer invoking the provisions of section 14A r.w.r 8D of the Act has computed the disallowance at Rs.1,66,51,972/-. Before the learned Commissioner of Income Tax (Appeals) the assessee had argued that since the appellant is in pre-operative stage, all the expenditure incurred is to be capitalized therefore there is no possibility for disallowing of any expenditure related to earning of any exempt income. Further, it was argued before the learned Commissioner of Income Tax (Appeals) that the entire investment was made in “growth Mutual Funds” which generates only capital gain/loss on sale of such investment and therefore provisions of section 14A will not be applicable. The learned Commissioner of Income Tax (Appeals) after considering the arguments of the Ld.A.R., has remitted the matter back to the file of learned Assessing Officer for verifying the claim of the appellant whether the investments were made in “growth Mutual Funds” as claimed by the

Ld.A.R., because the details of such investments were not before the learned Commissioner of Income Tax (Appeals), and if found so, directed the Ld.A.O., to delete the addition made under section 14A of the Act by agreeing with the arguments of the learned Authorized Representative. We find merit in the order of the learned Commissioner of Income Tax (Appeals) on this issue. If investments are made in “growth mutual funds” yielding only capital gain/loss which is taxable income under the head ‘Capital Gain”, then the provisions of section 14A will not be applicable because provisions of Section 14A deals with expenditure incurred in relation to income not includible in total income, needless to mention that expenditure incurred in such situation will go to add to the cost of asset wherein provisions of Section 14A of the Act will not be applicable. Since the learned Commissioner of Income Tax (Appeals) has only remitted back the matter to the file of the learned Assessing Officer for verifying the mode of investment and decide according to the above ratio laid down, we do not find it necessary to interfere with his order on this issue also.

7. In the result, the appeal of the Revenue is dismissed.

Order pronounced in the open court on the 9th September, 2016

(एन.आर.एस. गणेशन)

(N.R.S.Ganesan)

न्यायिक सदस्य /Judicial Member

चेन्नई/Chennai,

दिनांक/Dated 9th September, 2016

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(ए. मोहन अलंकामणी)

(A. Mohan Alankamony)

लेखा सदस्य / Accountant Member

आदेश की प्रतिलिपि अग्रेषित/Copy to:

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|--------------------|-------------------------|------------------------------|
| 1. Appellant | 2. Respondent | 3. आयकर आयुक्त (अपील)/CIT(A) |
| 4. आयकर आयुक्त/CIT | 5. विभागीय प्रतिनिधि/DR | 6. गार्ड फाईल/GF. |