

**आयकर अपीलीय अधिकरण, 'डी' न्यायपीठ, चेन्नई**  
**IN THE INCOME TAX APPELLATE TRIBUNAL, 'D' BENCH, CHENNAI**  
**श्री एम बाला गणेश, लेखा सदस्य एवं श्री धुव्वुरु आर.एल रेड्डी न्यायिक सदस्य के समक्ष**  
**BEFORE SHRI M. BALAGANESH, ACCOUNTANT MEMBER AND**  
**SHRI DUVVURU RL REDDY, JUDICIAL MEMBER**

आयकर अपील सं./I.T.A.No.2486/CHNY/2017

(निर्धारण वर्ष / Assessment Year: 2013-14)

M/s. Nalli Trust, No.9, Nageswaran Road, T. Nagar, Chennai – 600 017.	Vs	The ACIT, Non-Corporate Circle 1(1), Chennai – 34.
PAN: AAATN0028K		
(अपीलार्थी/Appellant)		(प्रत्यर्थी/Respondent)

अपीलार्थी की ओर से/ Appellant by	:	Shri N. Devanathan, Advocate
प्रत्यर्थी की ओर से/Respondent by	:	Shri R.V. Aroon Prasad, JCIT

सुनवाई की तारीख/Date of hearing	:	04.06.2019
घोषणा की तारीख /Date of Pronouncement	:	07.06.2019

**आदेश / ORDER**

**PER M. BALAGANESH, ACCOUNTANT MEMBER:**

This appeal of the assessee arise out of the order of the Ld. Commissioner of Income Tax (Appeals)-2, Chennai vide proceedings in ITA No.35/CIT(A)-2/2016-17 dated 31.07.2017 for the assessment year 2013-14 against the of assessment passed by the Ld. ACIT, Non-Corporate Circle – 1(1), Chennai (herein after referred to as Ld. AO) u/s. 143(3) of the Income Tax Act,1961 (herein after referred to as the Act).

2. The first issue to be decided in this appeal is to whether the Ld.CIT(A) was justifying in upholding the disallowance of claim of business loss to the tune of Rs.30 lakhs on cancellation of lease deposit in the facts and circumstance of the case.

3. The ground Nos.1 &11 raised by the assessee are general in nature and does not require any specific adjudication.

4. The brief facts of the issue are that the assessee is a private trust assessed to tax in the capacity of "Association of Persons" (AOP). It is engaged in the retail business of textiles and jewellery. In addition to the business income derived thereon, the assessee had also disclosed income from house property and interest income.

5. The Ld.AO during the course of assessment proceedings on obtaining the details of administrative expenses, noticed that expenses of Rs.30 lakhs was debited as loss on cancellation of lease. The assessee was asked to explain the same. In response the assessee explained :-

*"The Assessee M/s. Nalli Trust entered into Lease Deed with Sri. A.C.Venkatarayalu son of Chinnasami and Smt. Santhanalakshmi wife of Kumarakrishnan for leasing the property for setting up a show room at*

*premises at No.213/221, Jawaharlal Nehru Street, Puducherry - 605001. The owner in the process of constructing the building, when the lease deed was entered. Infact, the owner was to construct the building as per the local authority and also with the suitable modification as requested by M/s. Nalli Trust.*

*However on completion of the building, the owner could not obtain the power connection for the building. The owner asked the assessee to commence the business with self generator power and pay the rent. The assessee is engaged in the business where lot of customers are particularly women. The assessee did not want to commence the showroom without a proper power connection and generator as a backup. Besides running a business with a generator will not be economical and the assessee will incur heavy loss.*

*The Assessee paid a advance of Rs.60 Lakhs. In order to avoid a protracted litigation and legal expenses time and money, the assessee reached a compromise with owner of the property and received back Rs.30 Lakhs out of the advance paid Rs.60 Lakhs. Hence the balance 30 Lakhs is treated as business expenses and written off.”*

6. The Ld. AO after going through the reply of the assessee and on perusal of the deed for surrender of lease, observed that the assessee was planning to take the property on lease for 27 years as per the original lease deed and that the amount of lease deposit provided shall be returned back after adjusting the expenditure incurred by the landlord which was fixed at Rs.30 lakhs. Accordingly, the Ld. AO concluded that the remaining balance of Rs.30 lakhs which was irrecoverable and not recovered by the assessee would

lead to loss arising on capital account transaction and accordingly not allowable as business loss. The Ld. AO furthered his contention by placing reliance on the fact that the lease deed also provide for construction of showroom building by the landlord in accordance with the specifications provided by the assessee therein. Based on this, the Ld. AO concluded that the entire transaction was on capital account and any loss arising on write-off of such capital deposit would result only in capital loss and hence not allowable as revenue loss in the hands of the assessee AOP. Accordingly the Ld. AO disallowed the sum of Rs.30 lakhs in the assessment. This action of the Ld. AO was upheld by the Ld. CIT(A). Aggrieved, the assessee is in appeal before us.

7. We have heard the rival submissions. The primary facts stated herein above remain undisputed and hence the same are not reiterated for the sake of brevity. The Ld. DR before us stated that the assessee had entered into lease deed for 27 years which itself proves that there is an enduring benefit to the assessee by paying the lease deposit of Rs.60 lakhs. And when there is a loss incurred by the assessee due to irrecoverability of such deposit partially, the same would have to be treated only as capital loss and accordingly

prayed for non-interference in the order of the lower authorities. The Ld. DR placed reliance on the decision of the Hon'ble Supreme Court in Hasimara Industries Ltd., vs. CIT reported in 98 Taxman 303 (SC) in support of his contentions.

8. Per contra, the Ld. AR stated that the lease deed was not at all activated by the assessee. The assessee after paying the lease deposit of Rs.60 lakhs to the landlord was waiting to get possession from the landlord. The construction of the building was to be carried out by the landlord as per the specifications of the assessee and it is clearly mentioned in the lease deed that all necessary regulatory and Governmental approvals were to be obtained by the landlord for the subject mentioned premises taken on lease. It was argued since the assessee could not take over the possession of the property despite being completed due to non-availability of electricity connection from the Government for the subject mentioned premises, and in view of the fact that the assessee could not meet the request of the landlord to run the subject mentioned premises by using generator, the assessee chose to arrive at a compromise with the landlord pursuant to which the assessee could receive only Rs.30 lakhs out of the deposit paid to the landlord. It was pleaded that obviously the

landlord had indeed incurred expenditure in the subject mentioned premises by way of construction which had to be compensated by the assessee but since the assessee would also not get any return on that amount spent either in cash or in kind, there was no asset that was left with the assessee on cancellation of lease and hence there cannot be any enduring benefit that can fall on the assessee. Hence it was argued that the lease deposit written off was incidental to the carrying on the business of the assessee in opening various showrooms at various places in India. The Ld. AR placed reliance on the decision of the Hon'ble Supreme Court in the case of CIT vs. Mysore Sugar Co. Ltd., reported in 46 ITR 649 in support of his contentions. He also placed reliance on the decision of the co-ordinate Bench of the Delhi Tribunal in the case of FAB India Overseas India Pvt. Ltd., vs. ACIT in ITA No.199 & 672/Del/2012 dated 28.06.2013 and also on the decision of the Hon'ble Jurisdictional Madras High Court in the case of the M/s. Tamilnadu Magnesite Ltd., vs. ACIT in T.C. (Appeal) No.907 and 908 of 2007 dated 5<sup>th</sup> June 2018. At the outset we find that the decision relied upon by the Ld. DR on the Apex Court reported in 98 Taxmann 303 *supra* is factually distinguishable in view of the fact that in that case the sum of Rs.20 lakhs was deposited by that assessee with the

licensor company for the purpose of securing the license under which that assessee had acquired the right to work in the licensors cotton mills. This deposit was made as per the clause mentioned in leave and license agreement. There was a clear finding of fact in that case wherein which the deposit as required by the relevant clause has not been made by the assessee, then the assessee would not have secured the license of the cotton mill because at that time, the assessee was not doing any business in cotton. Hence the Hon'ble Apex Court observed that the deposit was clearly made for the purpose of acquiring of profit making asset to carry on business in cotton and accordingly the loss arising in thereon of such deposit cannot be held to be on revenue account and cannot be treated as business loss and had to be construed only as capital loss. The facts of the instant case before us are totally different from the facts that were before the Supreme Court *supra*. In the instant case, the lease deposit was made in the regular course of carrying on the business of textiles and jewellery by the assessee by opening a shop at Puducherry and as per the leave and license agreement, the landlord is supposed to carry out the construction as per the specifications of the assessee and obtain necessary regulatory approvals. The assessee had to terminate the lease due to non-performance of the

landlord by getting electricity connection for the subject mentioned lease premises and in that process, the assessee had to forego a regular business deposit of Rs.30 lakhs and consequently had to write-off the same in its books and claim the same as deduction. This, in our considered opinion, would have to be construed only as a loss incidental to the regular carrying on of normal business by the assessee allowable U/s.28 of the Act. In this regard, we find that the reliance placed by the Ld. AR in the decision of the Hon'ble Supreme Court in the case Mysore Sugar Co. Ltd., reported in 46 ITR 649 comes to the rescue of the assessee. The head notes of the said decision are reproduced herein under:-

*"LOSS — CAPITAL LOSS AND TRADING LOSS — COMPANY MANUFACTURING SUGAR — ADVANCE OF SEEDLINGS, FERTILISERS AND MONEY TO SUGARCANE GROWERS TO BE ADJUSTED TOWARDS PRICE OF SUGARCANE TO BE SUPPLIED LATER — LOSS THROUGH NON-DELIVERY OF SUGARCANE — WHETHER CAPITAL LOSS OR TRADING LOSS — WHETHER ALLOWABLE — INCOME-TAX ACT, 1922, ss. 10(2)(xi), 10(2)(xv)*

*The assessee who carried on the manufacture of sugar used to advance seedlings, fertilisers and money to sugarcane growers under an agreement by which the growers agreed to sell the next crop of the sugarcane grown by them exclusively to the assessee at current market rates and to have the advances adjusted towards the price of the sugarcane to be delivered to the company. In a certain year owing to drought the sugarcane growers could not grow sugarcane and the advances remained unrecovered. A Committee appointed by the Government recommended that the assessee should ex gratia forgo some of its dues. The assessee accordingly waived its right in respect of Rs. 2,87,422 and claimed this amount as a deduction under sections 10(2)(xi) and 10(2)(xv) of the Income-tax Act. The question was whether the amount of Rs. 2,87,422 which was given up represented a loss of capital or was a revenue expenditure:*

*Held, that so far as the assessee company was concerned it was merely making a forward arrangement for the next year's crops and paying an amount in advance out of the price; there was no element of a capital*



*investment in making the advance and the loss incurred by the assessee was, therefore, a loss on the revenue side and was deductible.”*

We also find that the Hon'ble Jurisdictional Madras High Court in the case of Tamilnadu Magnesite Ltd., had also adjudicated the similar issue wherein it was held as under:-

*“Claim of deduction / loss relating to the 'project expenses' in the computation of taxable total income - expenditure incurred by the assessee was revenue in nature and not capital - Whether the Tribunal is correct in concluding that the expenses were capital in nature even though such expenses were incurred for 'possible expansion' of the existing business? - Whether the Tribunal is correct in concluding that the expenses were capital in nature even though such expenses were incurred for 'possible expansion' of the existing business?*

*- Held that:- The assessee though had entered into arrangement with the banks and co-promoters and took action for acquisition of land, import of machineries, etc., no new venture was established by the assessee. The venture, which was to be taken over by the assessee and operated did not fructify, not on account of the conduct of the assessee, but on account of the decision of the Government of Tamil Nadu. In our considered view, the decision of the Government of Tamil Nadu to sell the project is a very important fact, which has to be borne in mind to decide as to whether the expenditure incurred by the assessee was capital or revenue in nature.*

*The Assessing Officer fell in error in going by the fact that the expenditure was incurred from the capital account forgetting that the test to be applied to ascertain as to whether the expenditure is revenue or capital is not based on where the funds were drawn from. The broad parameters and tests, which have been laid down by various decisions are that there should be an enduring benefit, which should accrue to the assessee and there should be a creation of a new asset. In the instant case, both these parameters remain unfulfilled. - Decided in favour of assessee”*

In view of the aforesaid findings in the facts and circumstances of the case and respectfully following the judicial precedents relied upon herein above, we held that the loss of Rs.30 lakhs on account of cancellation of lease should be treated as business loss of the assessee and accordingly the ground Nos. 2 to 6 raised by the assessee are allowed.

9. The next issue to be decided in this appeal is to whether the Ld. CIT(A) was justified in upholding the proportionate disallowance of interest on borrowed funds to the tune of Rs.12,98,006/- in the facts and circumstance of the case.

10. The brief facts of the issue is that the Ld. AO observed a sum of Rs.89.51 lakhs has been included as "Harvard University Remittance" under the head 'Advances and Deposits' corresponding to Nalli Silk Sarees, Delhi SE. The assessee explained that the said deposit was made on various dates during financial years 2009-10 to 2011-12 on account of higher education of Ms. Lavanya Ramanathan at Harvard University for acquiring professional qualification. It was further stated that the said amount was capitalized in the books of the

assessee and no deduction was claimed thereon. It was further stated that after finishing her course, Ms. Lavanya Ramanathan is working for the assessee AOP.

11. The Ld. AO has however observed that Ms. Lavanya Ramanathan was one of the beneficiaries of assessee's AOP and such payments made to beneficiaries cannot be allowed as business expenditure. But taking into consideration that no deduction was claimed by the assessee towards the payment of higher education fees of Ms. Lavanya Ramanathan, the Ld. AO observed that assessee on one hand had made borrowings and was paying interest on such borrowings but on the other hand had parted with the funds which were not relevant for the purpose of business of the assessee by parking it towards payment of fees of higher education of Ms. Lavanya Ramanathan. Hence this tantamounts to diversion of borrowed funds for non-business purposes and accordingly proportionate interest disallowance has to be made U/s.36(1)(iii) of the Act. The Ld. AO observed that the rate of interest on loans taken by the assessee was 14.5% and accordingly applied 14.5% on the amount shown under advances and deposits to the tune of Rs.89,51,763/- and disallowed proportionate interest U/s.36(1)(iii) of

the Act for the sum of Rs.12,98,006/- in the assessment. Before the Ld. CIT(A), the assessee explained that the assessee was having sufficient own funds which were much more than the borrowed funds and accordingly it had to be presumed that the said deposit in the form of higher education fees of Ms. Lavanya Ramanathan have been paid out of own funds of the assessee and not out of the borrowed funds. By placing reliance on the various decisions of High Courts and Supreme Court, the assessee pleaded for deletion of disallowance of interest. The Ld. CIT(A) further observed that the assessee was not able to prove that the amount paid to Harvard University were out of its own funds despite being given sufficient opportunities by the Ld. AO. The assessee pleaded before the Ld. CIT(A) that the borrowings made by the assessee are for specific business purposes and Ms. Lavanya Ramanathan was working in Nalli before she went to USA for higher studies and continue to work for Nalli after completing her Business Management Studies in USA after working for a short period with McKinsey & Co., Consultants in USA in order to gain experience with international firm. The Ld. CIT(A) further disregarded the entire contention of the assessee and upheld the action of the Ld. AO. Aggrieved, the assessee is in appeal before us.

12. We have heard the rival submissions and perused the materials available on record. The facts stated herein above remain undisputed and hence the same are not reiterated herein for the sake of brevity. We find from the perusal of the Balance Sheet of the assessee for the year ended 31.03.2016 that it has got capital account balance of Rs.1.51 crores and reserves of Rs.77.32 crores. We find from the perusal of the Balance Sheet that borrowings of the assessee is close to Rs.98 crores which is more than own funds. Hence various decisions relied by the Ld.AR in the case law compilation does not come to the rescue of the assessee. But we find that there is no dispute that Ms. Lavanya Ramanathan was a family member of the Managing Trustee of the assessee's AOP (trust) and is one of the five beneficiaries in the said AOP and there is no dispute that she was working with Nalli before going for her higher studies in USA. And it is not in dispute that after her higher studies and after a brief stint in M/s. McKinsey & Co. Consultants, USA , had indeed come back to India and started working for Nalli. It is in everybody's knowledge that one of the primary advantage or tagline of Harvard Business School, USA is that they groom the students to generate self employment and become entrepreneurs themselves and not merely students as management executive or employee.

Hence the assessee was able to prove the business nexus and the commercial expediency in this entire transaction to drive home the fact that the said payment of fees of higher education to Harvard University, USA on account of Ms. Lavanya Ramanathan was for business purpose of the assessee. It is not in dispute that no deduction *per se* was claimed by the assessee in respect of this payment of fees to Harvard University but that does not rule out the very factum of payment being made for business purpose of the assessee. It is not in dispute before us that Ms. Lavanya Ramanathan after her higher studies had started working for the assessee and assessee was benefited drastically by her business sense and quick decision making process.

13. One of the primary requirement of making disallowance U/s.36(1)(iii) of the Act is that the borrowed funds should have been utilized for non-business purposes. In the instant case, we have already held that the payment of higher education fees to Harvard University, USA is for business purposes only. Hence we hold that no disallowance of interest U/s.36(1)(iii) of the Act could become operational. Accordingly the Ground Nos. 7 to 10 raised by the assessee are allowed.

14. In the result the appeal of the assessee is allowed.

Order pronounced on the 7<sup>th</sup> June, 2019 at Chennai.

Sd/-

(धुव्वुरु आर.एल रेड्डी)  
(Duvvuru RL Reddy)  
न्यायिक सदस्य/Judicial Member

Sd/-

(एम बाला गणेश)  
(M. Balaganesh)  
लेखा सदस्य /Accountant Member

चेन्नई/Chennai,

दिनांक/Dated 7<sup>th</sup> June, 2019

**RSR**

आदेश की प्रतिलिपि अग्रेषित/Copy to:

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