IN THE HIGH COURT OF JUDICATURE AT BOMBAY

ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO.330 OF 2012

Commissioner of Income Tax-2,
Mumbai 400 020 ...Appellant
v/s
HDFC Bank Ltd. ...Respondent

Mr Suresh Kumar for the Appellant.
Mr J.D. Mistry, Sr. Counsel with Mr Atul Jasani for the Respondent.

CORAM : S.C. DHARMADHIKARI AND
B.P. COLABAWALLA JJ.

Reserved on : 10th July 2014.
Pronounced on : 23rd July 2014.

JUDGMENT ***[Per B.P. Colabawalla J.]*** :-

1. This Appeal under section 260A of the Income Tax Act 1961, has been filed by the Commissioner of Income Tax-2 challenging the order passed by the Income Tax Appellate Tribunal (hereinafter referred to as the ITAT) dated 29th June 2011. By the impugned order, the ITAT dismissed the Appeal filed by the Revenue in relation to Assessment Years 2001-02, 2002-03, 2003-04, 2004-05 and 2005-06.

2. Mr Suresh Kumar, the learned counsel appearing on behalf of the Appellant, submitted that the impugned order passed by the ITAT requires

interference and gives rise to substantial questions of law that need to be answered by this Court and read as under :-

> *"(A) Whether on the facts and in law, the Hon'ble Tribunal was correct in holding that the investment in tax free securities/investments are represented by assessee's own funds in the shape of share capital and reserves, ignoring the fact that the assessee is a bank involved in transactions of money in various forms and treasury operations is only out of its functions ?*
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> *(B) Whether the ITAT was correct in law in holding that the broken period interest is allowable as a deduction, inspite of the Hon'ble Supreme Court's decision in the case of CIT v/s Vijay Bank (187 ITR 541) and the Rajasthan High Court's decision in the case of Bank of Rajasthan (316 ITR 391) ?*
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> *(C) Whether the ITAT is right in law in holding that the assessee is entitled for deduction with respect to the diminution in value of the investment and amortization of premium on investment held to maturity on the ground of mandate by RBI guidelines thereby ignoring the decision of the Supreme Court in the case of Southern Technologies vs. CIT (320 ITR 577) ?"*

3. With reference to question (A), Mr Suresh Kumar submitted that the ITAT erred in holding that the investments of the Assessee in tax free securities / investments were from the Assessee's own funds. Since the Assessee had paid interest on borrowed funds and and the Assessee's own funds were not separately identified, the investment in Government securities had been made by the Assessee Bank from common pool of funds available with it. According to Mr Suresh Kumar, as per the provisions of section 14A, no deduction could be allowed in respect of expenditure incurred by the Assessee against the income claimed as exempt from tax, as apportionment of expenditure was an inherent part of section 14A. He submitted that in the absence of a direct nexus between Assessee's own

funds and the investment made by it, the investment ought to be treated from the common pool having both borrowed as well as own funds of the Assessee and therefore, proportionate disallowance of interest by the Assessing Officer was fully justified. He therefore submitted that the CIT (Appeals) & the ITAT had gone wrong on this count that required interference by this Court.

4. We do not agree. In the case at hand, as recorded by the ITAT, undisputedly the Assessee's own funds and other non-interest bearing funds were more than the investment in the tax free securities. The ITAT therefore held that there was no basis for deeming that the Assessee had used the borrowed funds for investment in tax free securities. On this factual aspect, the ITAT did not find any merit in the contention raised by the Revenue and therefore, accordingly answered the question in favour of the Assessee. On going through the order of the CIT (Appeals) dated 28th March 2005 as well as the impugned order, we do not find that the CIT (Appeals) or the ITAT erred in holding in favour of the Assessee. In this regard, the submission of Mr Mistry, the learned Senior Counsel appearing on behalf of the Assessee, that this issue is squarely covered by a judgment of this Court in the case of ***Commissioner of Income Tax v/s Reliance Utilities and Power Ltd., reported in (2009) 313 ITR 340 (Bom)*** is well founded. The facts of that case were that the Assessee viz. M/s Reliance Utilities and Power Ltd. had

invested certain amounts in Reliance Gas Ltd. and Reliance Strategic Investments Ltd. It was the case of the Assessee that they themselves were in the business of generation of power and they had earned regular business income therefrom. The investments made by the Assessee in M/s Reliance Gas Ltd. And M/s Reliance Strategic Investments Ltd. were done out of their own funds and were in the regular course of business and therefore no part of the interest could be disallowed. It was also pointed out that the Assessee had borrowed Rs.43.62 crores by way of issue of debentures and the said amount was utilised as capital expenditure and inter-corporate deposit. It was the Assessee's submission that no part of the interest bearing funds (viz. Issue of debentures) had gone into making investments in the said two companies. It was pointed out that the income from the operations of the Assessee was Rs.313.53 crores and with the availability of other interest free funds with the Assessee the amount available for investments out of its own funds were to the tune of Rs.398.19 crores. In view thereof, it was submitted that from the analysis of the balance-sheet, the Assessee had enough interest free funds at its disposal for making the investments. The CIT (Appeals) on examining the said material, agreed with the contention of the Assessee and accordingly deleted the addition made by the Assessing Officer and directed him to allow the same under the provisions of the Income Tax Act, 1961. The Revenue being aggrieved by the order preferred an Appeal before the ITAT who upheld the order of the CIT (Appeals) and

dismissed the Appeal of the Revenue. From the order of the ITAT, the Revenue approached this Court by way of an Appeal. After examining the entire factual matrix of the matter and the law on the subject, this Court held as under :-

> *"If there be interest-free funds available to an assessee sufficient to meet its investments and at the same time the assessee had raised a loan it can be presumed that the investments were from the interest-free funds available. In our opinion, the Supreme Court in East India Pharmaceutical Works Ltd. v. CIT (1997) 224 ITR 627 had the occasion to consider the decision of the Calcutta High Court in Woolcombers of India Ltd. (1982) 134 ITR 219 where a similar issue had arisen. Before the Supreme Court it was argued that it should have been presumed that in essence and true character the taxes were paid out of the profits of the relevant year and not out of the overdraft account for the running of the business and in these circumstances the appellant was entitled to claim the deductions. The Supreme Court noted that the argument had considerable force, but considering the fact that the contention had not been advanced earlier it did not require to be answered. It then noted that in Woolcombers of India Ltd.'s case (1982) 134 ITR 219 the Calcutta High Court had come to the conclusion that the profits were sufficient to meet the advance tax liability and the profits were deposited in the over draft account of the assessee and in such a case it should be presumed that the taxes were paid out of the profits of the year and not out of the overdraft account for the running of the business. It noted that to raise the presumption, there was sufficient material and the assessee had urged the contention before the High Court. The principle, therefore, would be that if there were funds available both interest-free and over draft and/or loans taken, then a presumption would arise that investments would be out of the interest-free funds generated or available with the company if the interest-free funds were sufficient to meet the investment. In this case this presumption is established considering the finding of fact both by the Commissioner of Income-tax (Appeals) and the Income-tax Appellate Tribunal."*
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> (emphasis supplied)

5. We find that the facts of the present case are squarely covered by the judgment in the case of ***Reliance Utilities and Power Ltd. (supra)***. The finding of fact given by the ITAT in the present case is that the Assessee's own funds and other non-interest bearing funds were more than the investment in the tax-free securities. This factual position is not one that is

disputed. In the present case, undisputedly the Assessee's capital, profit reserves, surplus and current account deposits were higher than the investment in the tax-free securities. In view of this factual position, as per the judgment of this Court in the case of ***Reliance Utilities and Power Ltd. (supra)***, it would have to be presumed that the investment made by the Assessee would be out of the interest-free funds available with the Assessee. We therefore, are unable to agree with the submission of Mr Suresh Kumar that the Tribunal had erred in dismissing the Appeal of the Revenue on this ground. We do not find that question (A) gives rise to any substantial question of law and is therefore rejected.

6. Even as far as question (B) is concerned, we find no infirmity in the orders passed by the CIT (Appeals) or the ITAT. In deciding this issue, CIT (Appeals) and the ITAT have merely followed the judgment of this Court in the case of ***American Express International Banking Corporation v/s Commissioner of Income Tax, reported in (2002) 258 ITR 601***. On going through the said judgment, we find that question (B) reproduced above and projected as substantial by Mr Suresh Kumar is squarely answered by the judgment of this Court in the case of ***American Express International Banking Corporation (supra)***. In view thereof, we do not find that even question (B) gives rise to any substantial question of law that needs to be answered by this Court.

7. As far as question (C) is concerned, we find that an identical question of law was framed and answered in favour of the Assessee by this Court in its judgement dated 4th July, 2014 in ***Income Tax Appeal No.1079 of 2012, Commissioner of Income Tax-2 v/s M/s Lord Krishna Bank Ltd. (now merged with HDFC Bank Ltd.).*** Mr Suresh Kumar fairly stated that question (C) reproduced above is covered by the said order. In view thereof, we are of the view that even question (C) does not raise any substantial question of law that requires an answer from us.

8. For all the aforesaid reasons, we find no merit in this Appeal. It raises no substantial question of law and is therefore dismissed. No order as to costs.

(B.P. COLABAWALLA J.) (S.C. DHARMADHIKARI J.)