

**IN THE INCOME TAX APPELLATE TRIBUNAL  
“C” BENCH : BANGALORE**

BEFORE SHRI GEORGE GEORGE K., VICE PRESIDENT  
AND  
SHRI LAXMI PRASAD SAHU, ACCOUNTANT MEMBER

ITA No.105/Bang/2023
Assessment year : 2015-16

M/s. Manipal Education and Medical Group India Pvt. Ltd., 24/1, 15 <sup>th</sup> Floor, JW Marriot, Bangalore – 560 001. <b>PAN : AADCM 8103A</b>	Vs.	The Deputy Commissioner of Income Tax, Circle 4(1)(2), Bangalore.
APPELLANT		RESPONDENT

Appellant by	:	Shri S.K. Tulsiyan, Advocate Ms. Bhoomija Verma, Advocate
Respondent by	:	Dr. Satyasai Rath, CIT(DR), Bengaluru.

Date of hearing	:	16.08.2023
Date of Pronouncement	:	29.08.2023

**ORDER**

*Per Laxmi Prasad Sahu, Accountant Member*

This appeal by the assessee is against the DIN & Order No.ITBA/NFAC/S/250/2022-23/1048076649(1) dated 19.12.2022 of the CIT(Appeals), National Faceless Appeal Centre, Delhi [NFAC] for the AY 2015-16.

2. The issues raised in this appeal are with regard to disallowance u/s. 14A and disallowance u/s. 36(1)(iii) of the Act. The brief facts of the case are that the assessee is engaged in the business of providing

engineering asset management and maintenance service. The assessee filed return of income on 30.09.2015 declaring loss of Rs.16,03,67,750. The case was selected for scrutiny and statutory notices were issued to the assessee. The assessee had specified domestic transactions but no adjustment was suggested by the TPO u/s. 92 of the Act. The AO noted that the company has made non-current investments of Rs.40,48,46,386 in equity shares and current investments of Rs.7,41,52,285. The company received dividend income on current investments of Rs.1,25,63,095 which is exempt income under the Act. Hence the AO applied section 14A and observed that the assessee has not reported any expenditure attributable to investment made to earn such exempt income. In this regard, the assessee was asked to provide note on applicability of section 14A along with computation of disallowance u/s. 14A r.w. Rule 8D. In response the assessee furnished working of disallowance u/s. 14A @ 0.5% of average investment amounting to Rs.27,36,547 and submitted that the dividend income was earned on shares & mutual funds claimed as exempt u/s. 10(34) & 10(35) of the Act and these investments were made out of own funds, therefore no disallowance was warranted u/s. 14A. The AO noted that the assessee has made fresh investments during the year and the assessee must have employed manpower either own or consultant. He examined the issue in the light of section 14A and found that the assessee has not satisfied correctness of expenditure relating to earning of exempt income. The AO proceeded to calculate disallowance & considered the entire average value investments i.e.,

current & non-current investments and accordingly calculated the disallowance as per Rule 8(2)(iii) at Rs.27,36,547.

3. The AO further noted that the assessee has debited a sum of Rs.2,86,38,749 into P&L account towards loan processing charges. On perusal of details submitted by the assessee, he observed that the loan processing charges were paid for loan for acquiring of capital assets and therefore not allowed as revenue expenditure and added to total income of the assessee.

4. The Addl. CIT after examining the records issued directions u/s. 144A of the Act to complete the assessment on the issues mentioned therein which are reproduced as under:

“1. Disallowance of interest u/s 36(1)(111):-

The following issue has been raised in the letter dtd: 04.12.2018 issued from this office on above issue.

"it is seen from the depreciation chart that you have shown addition of Rs. 14,44,37,222/- under the head building and Rs. 541, 76,651/- under the head Furniture Fixture and Electrical Fixture and Rs. 454,96,412/- under the head plant, Machinery etc. Thus the total addition of fixed asset during the year which was used for more than 180 days, is Rs. 24,59,28,739/- and which was used less than 180 days is Rs. 145,96,971/-. It is seen from the detail submitted before the AO that you have taken term loan from IDFC Ltd of Rs. 274 Crore and Rs. 37.16 Crore from Aditya Birla Finance Ltd. on which interest of Rs. 26,81,46,091/- and Rs. 459,88,666/- has been debit in account respectively. The copy of Loan sanction document of IDFC Ltd. has been filed which shows that the amended agreement was signed on 24.03.2014. Similarly, the agreement with the Aditya Birla Finance Ltd. is found to be signed on 09.05.2015 for the increase in term loan from Rs. 30 Crore to Rs. 58.3 Crore.

It is seen from the balance sheet that there is increase in the Long Term Borrowing by Rs. 125 Cr in comparison to last year and increase in reserve and surplus by Rs. 2.76 Cr. This increase is represented in asset side by increase in capitol work in progress by Rs. 90 Cr and tangible assets by Rs. 59 Cr and some investments have been sold. The increase in fixed assets includes Rs. 45 Cr of land which was purchased by the Company by taking term loan from Aditya Birla Finance Ltd. and interest of Rs. 2.76 Cr has been debited in this account towards the term loan which is used for purchase of land. The interest of Rs. 2.76 Cr on this loan is not an allowable revenue expenditure u/s 36(1)(iii) and necessary direction will be given to the AO to capitalize it in cost of the land.

You have debited Rs. 26.18 Cr as interest payable by the Company on IDFC rupee loan U/s 36(1)(iii). AS explained above the 90 Cr out of loan of Rs. 274 Cr has been shown as capitol work in progress. Hence, the proportionate amount of interest amounting to Rs. 8.8 Cr [ $\text{Rs. } 90\text{Cr} \times \text{Rs. } 26.81/\text{Rs. } 274\text{Cr}$ ] is to be disallowed as capital in nature as the addition is still in capital work in progress stage. Necessary direction will be given to the AO to disallow the above interest Rs. 8.8 Cr u/s 36(1)(iii) of the IT Act as treating it as capital in nature.

It is seen from the account that the opening WDV towards fixed assets is Rs. 208 Cr in the fixed asset schedule. You have taken loan of Rs. 274 Cr. from the IDFC Ltd. for the hostel project in Jaipur and other places. You are given an opportunity to explain where the amount of loan taken by the Company, sanctioned on 24.03.2014 has been utilized for the business purpose. You are given an opportunity to explain the utilization of loan from IDFC Ltd for business purpose."

The assessee has submitted the objection vide his letter dtd:10.12.2018 which is as under:

"As you are aware the company was engaged in the business of construction of hostels for the students who are studying in various Educational Institutions. Once the building is constructed the hostel room rent is collected by M/s. Manipal Integrated Services Private Limited. Thus the surplus for M/s.

Manipal Integrated Services Private Limited is the amount remaining after paying the interest on loan and other expenses of the project.

(i) One of the conditions of the Financial Institution is the hostels that are being provided should be ready and only after demonstrating that their revenue is assured with hostel building and students being filled in the financial Institutions provided loan to the company. Thus the financial Institutions insist on capital being brought in by the management of M/s. Manipal Integrated Services Private Limited to be used for constructions of hostel building.

During 2013-14, Compulsory Convertible Debentures of Rs. 100 crores were issued by the Company. Thus capital contribution is the form of CCD was brought in by the management before loans are given.

Two projects were constructed by M/s. Manipal Integrated Services Private limited is Jaipur phase 1 and Jaipur phase 2. The details are given below.

<i>Building A/c</i>		
<i>Building and other assets capitalised</i>	<i>Phase 1</i>	<i>Phase 2</i>
<i>01-04-2014</i>	<i>229 cr</i>	<i>-</i>
<i>Add capitalised</i>	<i>25 cr</i>	<i>-</i>
<i>Closing Balance</i>	<i>254 cr</i>	<i>-</i>
<i>Capital Work in progress</i>		
<i>Capital Work in progress</i>	<i>Phase 1</i>	<i>Phase 2</i>
<i>01-04-2014</i>	<i>16</i>	<i>Cr</i>
<i>Additions during the year</i>	<i>9 Cr</i>	<i>106 Crores</i>
<i>Less capitalised</i>	<i>25 Cr</i>	<i>-</i>
<i>Closing Balance</i>	<i>Nil</i>	<i>106 Crores</i>

Thus from the above it is very apparent that only Rs. 9 crores was used towards Capital Work in Progress of phase-1, which was funded from CCD. The initial loan taken along with CCD was used for Building which was capitalized Phase 1. The amount was replaced by the loan which was sanctioned. The amount of Rs. 100 crore of CCD was further used to construct the capital work in progress of phase 2 along with Internal accruals.

Thus we would like to inform that the total loan taken from banks are fully used for projects that are completed and the Interest that is paid should be allowed as Revenue Expenditure.

(ii) As regard Interest paid on the land purchase of Rs. 2.76 crore, we would like to inform that the land is already purchased/asset put to use and the interest paid on such loan as per various High Court decisions laws can be claimed as deduction. Hence, we feel the same should not be disallowed.

(iii) With regard to your query on disallowance of Interest of Rs. 8.8 crores, please refer to our replies in point 1, and hence we feel the Interest paid should be allowed as a deduction."

The assessee has filed further subincision on 12.12.2018 which is as under:

'This is further to the Income Tax scrutiny of one of our clients M/s. Manipal Integrated Services Private Limited and show cause notice received from your office vide letter dated 04-12-2018 We submit herewith additional clarifications further to our letter: submitted on 10-12-201. With regard to your query on how the loan sanctioned from financial institutions are utilized, we submit the following:

*Amounts in Cr.*

<i>Loan Sanctioned From</i>	<i>Balance as on 31-03-2014</i>	<i>Balance as on 31-03-2015</i>
<i>IDFC-Term Loan</i>	<i>168.00</i>	<i>274.00</i>
<i>Aditya Birla-Unsecured Loan</i>	<i>14.81</i>	<i>13.91</i>
<i>Adityo Birla- Secured Term Loan</i>	<i>20.00</i>	<i>18.49</i>
<i>Aditya Birla- Secured Term Loan</i>	<i>-</i>	<i>4.75</i>

CCD	-	-
TOTAL	202.81	311.15

The loans sanctioned during 20.13-14 were fully utilized for the Phase 1 of the Hostels and the balance amount for the Building were funded from CCD that were issued.

During the relevant period i.e A.Y 2015-16 (F Y 2014-15) an additional loan of Rs.128.35 cr was sanctioned from IDFC which was used for the following purpose:

Purchase of Land	Rs.45.04 CR
Replacing of CCD that was used for Construction of Phase 1 & 2	
Phase 1	Rs.46.32 CR
Phase 1	Rs.25.78 CR
Used for working Capital	Rs.11.20 CR
<u>Total</u>	<u>Rs.128.34 CR</u>

Thus from the above and as per the Conditions Precedent that were agreed between the Financial Institutions and MIs. Manipal Integrated Services Private Limited, the amount for construction is to be brought in by M/s. Manipal Integrated Services Private Limited upfront and the Term loan that is sanctioned is to be used to replenish the CCD that is used for construction. Thus we would like to mention that no Loan is used towards construction of the building and the entire interest should be allowed as Revenue Expenditure."

The submission filed by the assessee is also enclosed herewith. The assessee has also filed a Cash flow statement to explain the utilization of loan from IDFC of Rs. 274 Cr. and loan for Aditya Birla Finance Ltd.

A. It is seen from the submission of the assessee that the assessee has claimed to have utilized Rs. 45.04 Cr. to purchase a land in the month of May 2014 in which the part of the loan

taken from the IDFC @ 11.75% per Annum, has been used. It is found from the submission filed by the assessee on 12.12.2018 that out of fresh loan taken this year of Rs. 128.35 Cr from IDFC. It was utilized in the manner mentioned above. It is seen from the balance sheet of the Company that the long term loan has increase to 406 Cr from 281 Cr that means there is increase of 125 Cr. from the IDFC and Aditya Birla Finance Ltd. and other Creditors instead of Rs. 128.35 Cr claimed by the assessee in submission dtd: 12.12.2018. The loan taken from IDFC Ltd. was for the construction of the hostel in Jaipur as per the agreement but 45.04 Cr has been invested in the land at Eden in the month of May 2014. The assessee is not in the business of trading of land and this land has been purchased as investment. Hence, proportionate amount of interest @ 11.75% is treated as capital in nature. Hence, for 11 months the interest on Rs. 45.04 Cr. works out to Rs. 4.85Cr.  $[(45.04 \times 0.1175) \times 11/12]$ , which is added to the total income treating the same as incurred for capital asset.

You are directed to capitalize the amount of interest of Rs. 4.85 Cr. in the hands of the Company, by adding it to total income.

B. The assessee had shown capital work in progress of Rs. 106 Cr. during the year. It is submitted by the assessee that it has used CCD of 100 Cr. which was partly utilized in Phase-i of the Jaipur hostel and after release of 125 Cr. loan from IDFC Rs. 46.32 has been used to replace the CCD which was used in Phase-1 of the hostel project of Jaipur. Thus the assessee has used 6 Cr. from IDFC Lon in the capital work in progress on which 11.75% of interest has been paid.

In addition to that the assessee has also invested Rs. 25.78Cr. in Phase-1 of the hostel project which has been capitalized in this year. The assessee has shown Rs. 16 Cr. in capital work in progress as on 31.03.2014. The 2<sup>nd</sup> phase of the loan from IDFC has been received on 29/30.03.2014. Hence closing capital work in progress as on 31.03.2014 has been constructed either from CCD/own resource/1<sup>st</sup> Phase loan of IDFC and only 9 Cr used in this year has been used from phase-2 of IDFC loan which has been capitalized. Hence interest on Rs. 16 Cr. shown as used from Phase-2 loan of IDFC is not acceptable. It is presumed that the Rs. 16 Cr. which is shown in



the Cash flow statement of Phase-2 loan of IDFC is towards part of capital work in progress of Rs. 106 Cr as on 31.03.2015 shown in balance sheet. Hence, total investment in capital work in progress as on 31.03.2015 from Phase-2 loan of IDFC comes to Rs.22 Cr (Rs. 16 + Rs. 6). The interest @ 11.75% on Rs. 22 Cr is required to be capitalized. The interest amount works out to Rs. 2.585 Cr.( Rs. 22 x 0.1175). You are directed to disallow the above amount of Rs. 2.585 Cr. u/s 36(1)(iii) of the IT Act.

Thus the total amount of interest to be capitalized u/s 36(1)(iii) comes to Rs. 7.435 Cr(Rs. 4.85 Cr.+Rs. 2.585 Cr.). You are directed to add this amount to the total income u/s 36(1)(iii) of the IT Act treating the same as capital in nature. The above direction is given u/s 144A of the IT Act 1961 on the above issues.

.....”

5.2 In view of above direction, of the Addl. Commissioner of Income tax, Range-4(1), Bengaluru, issued u/s 144A of the IT Act, RS.7.435 Cr(Rs. 4.85 Cr.+Rs. 2.585 Cr.) is being treated as capital in nature and is being added to the total income u/s 36(1)(iii) of the IT Act.

(Addition: Rs. 7,43,50,000/-)”

5. As per the above directions, addition was made towards disallowance u/s. 36(1)(iii) of Rs.7,43,50,000. & the AO completed the assessment & returned loss was reduced to Rs. 5,46,42,454/-.

6. On appeal before the CIT(Appeals), the assessee submitted that no disallowance can be made u/s. 14A because the investments were made out of interest free funds and hardly any expenditure has been incurred either to make or maintain the investments as also to earn the income thereon. Further, with regard to disallowance u/s. 36(1)(iii), the assessee submitted that as per the agreed conditions between the

financial institutions and the assessee, the amount for construction is to be brought in by the assessee upfront and the term loan sanctioned is to be used to replenish the “Compulsory Convertible Debentures” that is used for construction. Hence the entire interest should be allowed as revenue expenditure. The loan was borrowed for business purpose and there is no distinction in section 36(1)(iii) between capital borrowed for revenue and capital asset purpose.

7. The CIT(Appeals) observed that the sum of Rs.45.04 crores sanctioned as loan from IDFC was used for purchase of land in May, 2014. The assessee was in the business of constructing hostel for students. The land was not utilized for business purpose of assessee, therefore interest of Rs.4.85 crores pertaining to loan used for purchase of land could not have been allowed u/s. 36(1)(iii) of the Act r.w. Explanation to section 43(1). The CIT(Appeals) relied on the decision of the Ahmedabad ITAT in Khyati Chemicals Private Ltd. v. DCIT (2002) 135 taxmann.com 200 (Ahmedabad Trib).

8. Further, the interest of Rs.2.585 crore paid to IDFC on loan of Rs.22 crore used for capital work in progress was also confirmed by the CIT(A).

9. Aggrieved from the order of the CIT(Appeals), the assessee is in appeal before the Tribunal.

10. Section 14A Disallowance: The Id. AR reiterated the submissions made before the CIT(Appeals) and submitted a written synopsis which is as under:-

“I. Sec.14A disallowance of expenditure income of Rs.27,36,547/- [See Ground No.1 and 2]

Per the Assessing Officer [A.O.] - the Assessee has made non-current investments of Rs.40,48,46,886/- in equity shares and current investments of Rs.7,41,52,285/- in unquoted shares, and has received exempt dividend income of Rs.1,25,63,095/- [See Para 3.1 of the Impugned Order in Original dated 21.12.2018].

Per the A.O., Sec.14A of the Act is applicable because the Assessee has not reported any expenditure attributable to investments made to earn such exempt income in the current year. Both the management of old and current investments requires application of mind, employed manpower either its own or any outside consultant — which would have resulted in some expenditure. The submission of the Assessee that the investment has been made from own funds is also rejected because it was verified from the audited accounts that no indirect interest pertaining to non-tax-exempt investments has been charged to the Profit / Loss Account. [See Para 3.3. of the Impugned Order in Original dated 21.12.2018].

OUR REBUTTAL:

The Assessee submits, that the disallowance by the A.O. of Rs.27,36,547/- on account of direct expenses pertaining to tax exempt investments made during the A.Y. — ought to be deleted because the Assessee has made the investments from sufficient 'interest free' own funds, evident from the Balance Sheet of the Assessee for the year ending 31.03.2015 [attached at Pg.6 of the Paper Book], and tabulated below for the sake of brevity and convenience:

S. No.	Particulars	Balance as on March 31, 2015 [INR]	Balance as on March 31, 2014 [INR]	Increment during the F.Y. ending March 31,2015 [INR]
1	Reserves and Surplus	28,54,56,386	25,78,23,977	2,76,32,409
2	Non-Current investments	40,48,46,386	38,37,43,311	2,11,03,075*
3	Current Investments	7,41,52,285	23,18,76,674	(15,77,24,389)**

\*Investment made during the year

\*\*Investments sold during the year ending March 31, 2015.

Thus, the interest free own funds available / at the disposal of the Assessee, stand at Rs.18,53,56,798/- being the total increment stemming from:

Increment of Rs.2,76,32,409 in the Reserves and Surplus, i.e., profit generated from operations for the F.Y. under consideration [See Schedule 4].

[+]

Increment of Rs.15,77,24,389/- stemming from the sale of current investments, i.e., mutual funds sold during the F.Y. under consideration [See Schedule 16].

Against this, the Assessee has only made a fresh investment of Rs.2,11,03,075/- for the F.Y. under consideration, i.e., equity investment qua purchase of non-cumulative optionally convertible preference shares in its subsidiary concern. [See Schedule 11].

Therefore, Section 14A of the Act is not applicable to the case at hand, considering the settled position of law enumerated in the decision of the Hon'ble jurisdictional Karnataka High Court [H.C.] in the case of CIT & Anr. Vs. Microlabs Ltd., [2017] 79 taxmann.com 365, that has held that when the investments have been made from a common pool of funds, and when the non-interest-bearing of the Assessee are more than the investment made in tax free securities — then Sec.14A is not applicable. ....

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This view finds further support in the decision of the Hon'ble Supreme Court [S.C.] in the case of CIT Vs. Reliance Industries Ltd. [2019 102 taxmann.com 52 (SC)] .....

.....  
Furthermore, the Assessee's appeal for the erstwhile A.Y. 2013-2014 in which a similar disallowance u/s 14A of the Act had been made by the A.O. - was deleted in favour of the Assessee by the Hon'ble jurisdictional Tribunal, on the basis of the same logic and reasoning. The matter of Sec.14A therefore stands covered in favour of the Assessee. The relevant excerpts of the decision rendered in Manipal Integrated Services Pvt. Ltd. vs. ACIT, ITA No.980/Bang/2018, decision dated 05.04.2019, are as under:

"9. We have considered the rival submissions. We find that as per Para 4 of the assessment order, it is stated by the AO that assessee has made investment of Rs. 51,76,46,752/ as per the balance sheet for the year ending 31.03.2013. In order to examine the applicability of this judgment of Hon'ble Karnataka High Court cited by Id. AR of assessee having been rendered in the case of CIT and Another Vs. Microlabs Ltd. (Supra), we examine the amount of interest free funds available with the assessee and compare it with investment in tax free securities. We find that assessee was having interest free own funds of Rs. 31,46,00,987/ in the form of share capital and reserves and surplus. In addition to that, the assessee is also having fund of Rs. 49,99,90,000/- in the form of CCDs on which no interest is being paid by the assessee. If we add up these two amounts, it is seen that total interest free funds available with the assessee is of Rs. 81,45,90,987/- as against the investment in tax free securities of Rs. 51,76,46,752/. Hence interest free funds available with the assessee is more than investment in tax free securities. In the light of these facts, now we examine the applicability of the judgment of Hon'ble Karnataka High Court rendered in the case of CIT and Another Vs. Microlabs Ltd. (supra). In this case, it was held by Hon'ble Karnataka High Court that when investments are made out of a common pool of funds and non-interest bearing funds were more than the investments in tax-free securities, no disallowance of interest expenditure u/s. 14A of the IT Act, 1961

can be made. No contrary judgment was cited by the learned DR of the revenue and therefore, we are duty bound to follow and apply this judgment cited by the learned AR of the assessee. We find that this judgment is squarely applicable in the present case and respectfully following the same, we hold that in the facts of the present case, it is to be presumed that the investment was out of interest free funds available with the assessee and therefore, no disallowance u/s. 14A r. w.r. 8D (ii) can be made out of interest expenditure.

10. This view of us finds support from a judgment of Hon'ble apex court rendered in the case of CIT vs. Reliance industries limited in Civil Appeal No. 10 to 13 of 2019 dated 02.01.2019, copy kept on record. In this case, it was noted by Hon'ble apex court that this is a finding of the tribunal that the interest free funds available to the assessee were sufficient to meet its investment and hence it could be presumed that the investment were made from the interest free funds available with the assessee. It was held by Hon'ble apex court that this is pure question of fact and since Hon'ble High Court in that case has decided the issue in favour of the assessee on the basis of finding of fact recorded by the tribunal, no interference is called for in the judgment of High court on this issue. Hence, it is seen that this judgment of Hon'ble apex court rendered in the case of CIT vs. Reliance industries limited (Supra) is on the same line as the judgment of Hon'ble Karnataka High Court rendered in the case of CIT and Another Vs. Microlabs Ltd. (supra).

11. Therefore, respectfully following this judgment of Hon'ble Karnataka High Court, we decide this issue in favour of the assessee and accordingly the disallowance of Rs. 92,71,233/-u/s. 14A r.w.r. 80(2)(ii) of IT Rules, 1962 is deleted and accordingly ground no. 2(b) is allowed. Regarding the second disallowance of Rs. 12,94,116/- u/s. 14A r.w.r. 8D(2)(iii) of IT Rules, 1962 being 0.5% of average investment, we hold that there is no infirmity in the order of CIT (A) in that regard because learned AR of the assessee has also fairly conceded in that regard. This disallowance of Rs. 12,94,116/- u/s. 14A r.w.r. 8D(2)(iii) of IT Rules, 1962 being 0.5% of average investment is upheld and accordingly, ground no. 2(c) is rejected.'

Accordingly, the disallowance of Rs.27,36,547/- by the A.O, and erroneously confirmed by the CIT(A) ought to be deleted, since the invocation of Sec.14A is not warranted.”

11. The Id. AR further submitted that the assessee has received dividend income only on the current investments which is clear from the audited financial statements and referred to Note No.16, 20 & 29. He produced a computation of disallowance under Rule 8D(2)(iii) and submitted that the maximum disallowance can be made of Rs.7,65,072 which is 0.5% of the average investments on which the assessee received exempt income. No exempt income was received on the non-current investments.

12. The Id. DR relied on the orders of the lower authorities.

13. After hearing the rival contentions, it is noticed from the assessment order that the AO has made disallowance under Rule 8D(2)(iii) on the entire average value of current and non-current investments, whereas as per Rule 8D(2)(iii), disallowance can be made only on such investments which has yielded exempt income. The assessee pleaded before the CIT(A) that no disallowance can be made because the assessee had own funds more than the investments made and no administrative expenditure was incurred. The CIT(A) confirmed the order of the AO. We observe from the financial statements that the assessee has received dividend income only on current investments and the computation of disallowance submitted by the Id. AR comes to Rs.7,65,072. However, we note from the order of the AO that during the course of assessment proceedings the assessee

itself submitted that dividend is earned on equity shares and mutual funds, but in the computation of disallowance submitted before us, only the average value of investments made in mutual funds has been considered. The disallowance under Rule 8D(2) (iii) should be made on the basis of average value of those investments in which the assessee has yielded exempt income. The Hon'ble High Court in the case of Cargo Motors (P.) Ltd. v. Deputy Commissioner of Income-tax reported in [2022] 145 taxmann.com 641 (Delhi) has settled this issue in favour of the assessee. The relevant part of the judgement is as under:-

*While section 14A is charging section, rule 8D is method/mechanism to determine the amount of expenditure incurred in relation to income, which does not form part of the total income of the assessee. By virtue of the charging section, namely, section 14A, the Assessing Officer has the power only to determine the amount of expenditure incurred in relation to such income which does not form part of the total income. [Para 13]*

*Rule 8D(2)(iii) clearly postulates that in calculation of the disallowance amount, 'an amount equal to one half per cent of the value of the investment, income from which does not or shall not form part of the total income' should be taken into consideration. Thus, it is not all investment but only that which is expressly spelt out in rule 8D(2)(iii) read with section 14A and rule 8D(i) which is to be reckoned for purpose of calculation of average of half per cent. [Para 14]*

*Consequently, only those investments are to be considered for computing average value of investments which yielded exempt income during the relevant assessment year. [Para 21]*

*Keeping in view the mandate of law, the question of law is answered in favour of assessee, as the Tribunal has erred in confirming the disallowance made under rule 8D by not restricting the disallowance to 0.5 per cent of those investment only where assessee had earned exempt income. [Para 23]*

Considering the above judgement & judgements relied by the Id. AR of the assessee, we remit this issue to the file of the AO for fresh computation of disallowance under Rule 8D(2)(iii) in terms of the



above judgment of Hon'ble Delhi High Court in the case of Cargo Motors (P.) Ltd. v. Deputy Commissioner of Income-tax cited supra. The assessee is directed to provide necessary documents in support of its claim and avoid seeking unnecessary adjournment for early disposal of the case. The AO shall grant reasonable opportunity of being heard to the assessee. Thus ground No. 02 is allowed for statistical purposes.

14. Disallowance u/s. 36(1)(iii) : The ld. AR reiterated the submissions made before the lower authorities and filed written synopsis as follows:-

**““Disallowance of interest amounting to Rs.7,43,50,000/- under Sec.36(1)(iii) of the Act [See Ground 3 and 4]**

The allegations qua the said disallowance under Sec.36(1)(iii) emanates from the erroneous understanding of the A.O. that loan taken by the Assessee from IDFC Bank has been utilized for the purpose of a) investment in land and b) as capital work in progress - thus the proportionate interest [on the loan amounts taken from IDFC Bank Ltd.] ought to have been capitalized since the assets involved has not been 'put to use' in the A.Y. under consideration and thus cannot be claimed as a legitimate deduction. [See Para 5 of the Impugned Order in Original].

To elaborate, the disallowance has been bifurcated into two parts by the Revenue, i.e.,

- a sum of Rs.4,85,00,000/- claimed by the Assessee as revenue expenditure has been disallowed by the A.O. [and confirmed by the CIT(A)] — on the erroneous basis that the Assessee is in the business of construction of hostels for students, and a fixed asset, i.e., land has been purchased from a loan of 45.04 Crs sanctioned from IDFC Bank. However, the land has not been utilized for business purpose. Therefore, the proportionate amount of interest has been calculated and disallowed. The CIT[A] has apart from Sec.36(1)(iii) also

referred to Explanation 8 to Sec.43(1) of the Act, to confirm the disallowance. [ This has been challenged by the Assssee via Ground No.3]

- a sum of Rs.2,58,50,00/- claimed by the Assessee as revenue expenditure has been disallowed by the A.O. [and confirmed by the CIT(A)] — on the erroneous basis that the Assessee has made a total investment in capital work in progress as on 31.03.2015 from a Phase No.2 Loan of IDFC that comes up to 22 Crs. 11.75% of interest on this was required to be capitalized, which has not been done by the Assessee, thus the same stands disallowed. [This has been challenged by the Assssee via Ground No.4]

#### OUR REBUTTAL:

Factually, it is submitted that the Assessee has taken only one borrowing from IDFC, i.e., a debt instrument, initially entered into on 19.06.2012, and revised during the F.Y. under consideration via revised Letter of Intent dated 14.03.2014 entered into between the Assessee and IDFC Company Ltd. [and attached to the Paper Book at Pgs. 41 to 62], whereby the Rupee Term Loan was reduced from Rs.600 Crores to 349 Crores. The nature of this borrowing was for the purpose of hostel project constructions as per speculations specified in the Letter of Intent.

The purpose behind such debt borrowing was centered around hostel development for the various universities of Manipal Group [as evident from Annexure li of the revised Letter of Intent at Pg.57 of the Paper Book].

The A.O. has disallowed the interest deduction claimed on the funds infused [via debt from IDFC] on the basis that the Proviso to Sec.36(1)(iii) which requires the capitalization of interest, till the date on which the asset has been put to use — and since, in this case, per the A.O., the asset has not been 'put to use' by the Assessee — the interest expenditure claimed is proportionally disallowed for the A.Y. under consideration.

At the outset it is firstly submitted that the Revenue nowhere disputes that the capital has been borrowed for the purpose of business — i.e., construction of hostels, and such purpose of

business had been carried on in the accounting year under question [evident from the Completion Certificate for Phase 1 dated 15.09.2015 attached herewith at Pgs.63 to 64 of the Paper Book]. It is pertinent to note that, in the case at hand, the hostel constructions [being purpose of business] has not only commenced and carried on in this F.Y. but also in previous accounting years, starting from F.Y. 2013, when the debt instrument was originally sanctioned by IDFC.

That said, the challenge to the disallowance of proportionate interest expenditure claimed by the Assessee vis-à-vis 'capital work in progress' — [See Ground No.4] is not being pressed, since such a similar disallowance has occurred in the previous A.Y. 2014-2015, and the Assessee has accepted / acceded to the same and chose not the challenge the same in appeal.

Now challenging the proportionate disallowance of interest expenditure qua the purchase of a fixed asset in the F.Y. under consideration via Ground No.3 [i.e., Land purchased, which is duly reflected in Schedule 10.1 of the Audited Accounts, at Pg.22 of the Paper Book] — it is at the outset submitted that the borrowed funds have not been utilized towards the acquisition of the Land in question, and the disallowance has been made by the Ld.A.O. on a presumptive basis, solely on surmises and conjectures.

It is further submitted that an advance for the purchase of the concerned fixed asset amounting to Rs. 40,20,00,000/- has been paid in the erstwhile financial year itself, i.e., F.Y. 2013-14 and forms part of the 'Capital Advance' declared in the said Financials. Attention in this respect is brought to Schedule 13 r/w Schedule 36 of the Audited Accounts of F.Y. 2013-14 at Pgs.85 and 101 of the Paper Book.

For the sake of brevity and convenience the tabulation of the advance payments made in F.Y. 2013-2014 amounting to Rs.40.20 Crs is reflected below, wherein the only tranche of payment made qua F.Y. 2014-2015 [A.Y. 2015-2016] i.e., the year under appeal is a sum of Rs.1.80 Crs (also evident from the table below):

S. No.	Sale Deed Number	Date of registration	Consideration	F.Y. in which payment made
1	1113/14-15	07.05.2014	11,16,00,000	2013-14
2	1115/14-15	07.05.2014	7,74,00,000	2013-14
3	1117/14-15	07.05.2014	11,10,00,000	2013-14
4	1119/14-15	07.05.2014	10,20,00,000	2013-14
5	1116/14-15	07.05.2014	1,80,00,000	2014-15
		<b>Total for [F.Y. 13-14]</b>	<b>40,20,00,000</b>	-
		<b>Total including [F.Y.14-15]</b>	<b>42,00,00,000</b>	

The Assessee submits that since the conveyances were executed and registered in F.Y. 2014-2015, the fixed asset was capitalized in F.Y. 2014-2015 for a total consideration of Rs.45.04 Crs, duly reflected as land purchased, visible from Schedule 10.1 of the Audited Accounts for F.Y. 2014-2015, at Pg.22 of the Paper Book. The total value of 45.04 Crs is inclusive of stamp duty and miscellaneous charges.

The Assessee reiterates that it has not utilized any borrowed funds towards making such advances for the purchase of the fixed asset in F.Y. 2013-2014. The source of the funds utilized towards acquisition of the fixed asset, is the additional Compulsory Convertible Debentures [CCDs] of Rs. 50,00,00,000/- issued to IDFC Private Equity Fund Ili vide an Agreement entered in F.Y. 2013-2014. The Loan for IDFC was qua hostel construction, and has been utilized only for that purpose, and not for the purpose of purchasing a fixed asset.

The addition of such interest free funds arising from the issuance of [CCDs] is visible from Schedule 5 of the audited financials for 2013-2014, at Pg. 62 of the Paper Book, and is reproduced herein below for the sake of brevity and convenience:

#### 5. Long-term borrowings

	Non-current portion		Current maturities	
	March 31,2014	March 31,2013	March 31,2014	March 31, 2013
<b>Debentures</b>				
Compulsory convertible debentures (CCDs)	99,99,90,000	49,99,90,000	-	-
	<b>99,99,90,000</b>	<b>49,99,90,000</b>	<b>-</b>	<b>-</b>
<b>Term loans</b>				
Term loans from financial institutions	1,81,99,13,217	30,00,00,000	81,95,285	

No addition to this effect has been made in the case of the Assessee, in the erstwhile A.Y. 2014-2015 [F.Y. 2013-2015]. Now, qua the remainder payment made in the A.Y. under consideration, A.Y. 2015-2016 [F.Y. 2014-2015], the same is also through the Assessee's own funds, since it held a sufficient opening cash balance, visible from Schedule 17 of the audited accounts for F.Y. 2014-2015 at Pg.6 of the Paper Book. Therefore, the Assessee has not utilized any borrowed funds towards the acquisition of the fixed asset either in the preceding A.Y. or even in this A.Y.

Even otherwise, as per law, the legal presumption that arises is that the investment in the land amounting to Rs.45.04 Crores has been made out of non-interest bearing funds, available with the Assessee. The stance of the Assessee is supported by the decisions of the Hon'ble Jurisdictional ITAT in the case of RNS Infrastructure Limited Vs. The DCIT, ITA No.1171/Bang/2022, decision dated 17.05.2023 which has held that when the Assessee has funds available that are both interest free and loans taken, then the presumption that would arise is that the investment in the capital asset has been made out of such interest free funds generated —when such interest free funds are sufficient to meet the investment in the capital asset.

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Furthermore, in the case of Bharath Fritz Werner Ltd. vs. The DCIT, [2023]146 taxmann.com 198 (Bangalore-Trib) — the Hon'ble jurisdictional Tribunal has further gone on to hold that in the event the capital asset stand purchased form a mixed bag of funds [comprising of own + borrowed funds], and the Assessee's own funds were substantial, then it was to be presumed that acquisition of fixed assets was out of own funds and proviso to section 36(1)(iii) could not be invoked to disallowed interest on borrowed loans. ....

.....

Accordingly, the disallowance of Rs.4,85,00,000/- by the A.O, that was erroneously confirmed by the CIT(A) - ought to be deleted, since the invocation of Sec.36(1)(iii) Proviso is not warranted, as the Assessee held sufficient funds 'interest free' funds to purchase the said Land.”

15. The Id. AR referred to the financial statements and submitted that the land purchase advance was given in the AY 2014-15 and the coordinate Bench in the assessee's own case (Manipal Integrated Services Pvt. Ltd.) for AYs 2013-14 & 2014-15 in ITA No. 979& 980/Bang/2018 dated 05.04.2019 held that CCDs loans raised during the year which are interest free and no interest bearing funds are utilised for earning exempt income. The assessee had CCDs of Rs. 99,99,90,000/- as on 31.03.2014. In the present case, the property was registered in the financial year 2014-15 and a small amount of Rs.1.80 crores was paid in the current financial year out of internal accounts. The loan from IDFC was for hostel construction and has been utilized only for that purpose and not for the purchase of land and the interest on such loan has been capitalized by the assessee.

16. The Id. DR relied on the orders of the lower authorities. He submitted that the Id. Addl. CIT has examined this issue and gave direction to the AO that the total amount of interest to be capitalized u/s. 36(1)(iii) which has been accordingly done by the AO and confirmed by the CIT(Appeals). Therefore the orders of authorities below should be upheld.

17. After hearing the rival contentions, we note from the record that the interest paid to IDFC of Rs.4.85 crores has been capitalized by the

AO by observing that the capital asset (land) purchased for which loan was taken, was not put to use in the business of the assessee and the assessee is not in the business of trading of land and this land has been purchased as investment, and therefore it should be capitalized u/s. 36(1)(iii) of the Act. The Addl. CIT in the 144A proceedings gave opportunity to the assessee to explain the utilization of loan from IDFC and treatment of interest paid on such loan. The assessee submitted reply on 10.12.2018 which is incorporated in his order. He observed that a sum of Rs.45.04 crores was utilized to purchase land from the part of fresh loan taken from IDFC & Aditya Birla Finance Ltd. and others of Rs.128.35 crores @ 11.75% since in the balance sheet of the company the long term loan has increased to Rs.406 crores from Rs.281 crores instead of Rs.128.35 crores claimed by the assessee. Accordingly the proportionate amount of Rs.4.85 crores was disallowed. The assessee in the written synopsis submitted that Rs.40.20 crores were paid in the FY 2013-14 which is clear from Note No.36 placed at PB page No. 101 of financial statement as on 31.03.2014 and Rs.1.80 crores was paid in the impugned FY 2014-15 and conveyance deed executed in May, 2014. We note from Schedule No.13 of the financial statement under sub-head 'Capital Advances' PB page No. 20 that the amount is reduced from Rs.54.17 crores to Rs.22.86 crores. The land appears in the Fixed Assets Schedule of the current year of Rs.45.04 crores under Note No.10.1 inclusive of stamp duty and miscellaneous charges. The reserves & surplus increased by Rs.2.76 crores from 37.68 to 40.44 crores. Current investments

decreased from Rs.23.19 to 7.42 crores which is source of cash. As per the cash flow statements the net cash & cash equivalent accrued are Rs.13.32 crores. As per Note No.04, the CCDs is of Rs. 99,99,90,000 out of Rs. 49,99,90,000 was raised upto 31.3.2013 and Rs.50 crores in 31.03.2014. The CCD is interest free as held by the coordinate Bench in the assessee's own case for AYs 2013-14 & 2014-15 (supra). We noted from the submission of the assessee that interest bearing funds have not been utilized for the purchase of land and the assessee had sufficient interest free funds and also observed by the coordinate bench in the assessee's own case for earlier AYs 2013-14 & 2014-15. The case law relied by the Id. AR of the assessee in his written synopsis supports the case of the assessee. After analysis of the above, we hold that the assessee has not utilized the borrowed fund for the purchase of land. The assessee has also sufficient opening cash balance as per Note No.17 and cash flow statement. Further, the assessee's submission that no interest bearing funds have been utilized is supported by the case laws referred by the assessee. Considering the entire facts and submissions, we hold that the land purchase by the assessee is out of non-interest bearing funds. Therefore the disallowance of interest of Rs.4.85 crores u/s 36(1)(iii) is not warranted and the same is deleted. We therefore allow ground No. 03 of the assessee.

18. The grounds No. 01 & 04 were not pressed by the Id. AR hence these grounds are dismissed as not pressed. The Ground Nos. 05 & 06



are general in nature, therefore, these are not required to be adjudicated.

19. In the result, the appeal of the assessee is partly allowed for statistical purposes.

Pronounced in the open court on this 29<sup>th</sup> day of August, 2023.

Sd/-

Sd/-

( GEORGE GEORGE K.)  
VICE PRESIDENT

(LAXMI PRASAD SAHU )  
ACCOUNTANT MEMBER

Bangalore,  
Dated, the 29<sup>th</sup> August, 2023.

*/Desai S Murthy/*

Copy to:

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR, ITAT, Bangalore.

By order

Assistant Registrar  
ITAT, Bangalore.