

[2019] 111 taxmann.com 269 (Bombay)

**INCOME TAX: Interest incurred on loans taken for acquiring controlling interest in company of same line, would be allowable expenditure under section 36(1)(iii)**

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[2019] 111 taxmann.com 269 (Bombay)

**HIGH COURT OF BOMBAY**

**Principal Commissioner of Income Tax, Mumbai**

**v.**

**Concentrix Services (I) (P.) Ltd.\***

M. S. SANKLECHA AND NITIN JAMDAR, JJ.

IT APPEAL NOS. 778 AND 867 OF 2017±

SEPTEMBER 4, 2019

**Section 36(1)(iii) of the Income-tax Act, 1961 - Interest on borrowed capital (For purpose of business) - Assessment years 2008-09 and 2009-10 - Whether interest expenditure and finance expenses incurred on loans taken for investment in acquiring controlling interest in a foreign subsidiary which was in same line of business as that of assessee so as to expand business in foreign country, would be allowable expenditure under section 36(1)(iii) - Held, yes [Para 6(f)][In favour of assessee]**

## **FACTS**

- The assessee was engaged in the business of providing information technology enabled services such as call centres, BPO services, etc.
- During relevant assessment years, the assessee had claimed expenses on account of interest and finance expenses as an allowable expenditure under section 36(1)(iii), which was in connection with loans taken from DBS Bank for acquisition of a Canadian company 'MC'.
- The Assessing Officer disallowed the interest and finance expenses on the ground that it was related to acquisition of shares of foreign subsidiary and not to the business of the assessee.
- On appeal, the Commissioner (Appeals) upheld the order of Assessing Officer for the assessment year 2008-09 but allowed deduction under section 36(1)(iii) for assessment year 2009-10.
- On appeal to the Tribunal, it held that acquisition of shares in a foreign subsidiary by assessee was for the purpose of its business and interest bearing funds were utilised for purchasing shares of foreign subsidiary through a special purpose vehicle and interest was paid on the loan and loss and gain in view of the foreign exchange variations was characterised as finance expenses. Therefore, interest paid on borrowed funds and finance expenses was allowed as a deduction under section 36(1)(iii).
- On revenue's appeal to the High Court:

## **HELD**

- It is undisputed that the business of the assessee is of running of BPO and Call Centres. Nor is it disputed that Canadian company is also in the business of Information Technology Enabled Services, i.e., BPO and Call Centre. It was the business decision of the assessee to enhance/expand its activities

and presence in the world market and for that purpose it had acquired controlling interest in the business of 'MC' which was in the same line of business as the assessee. To make the above investment for the purpose of its business, the loan was taken. Therefore, the interest expenditure incurred on loans taken for investment in acquiring controlling interest in a company which was in the same line of business as that of the assessee would be allowable expenditure under section 36(1)(iii). Where an assessee claims deduction of interest paid on capital borrowed, all that an assessee has to show is that the borrowed funds were used for business purpose and if so then interest will have to be allowed as a deduction. The submission on behalf of the revenue that the assessee is in the business of BPO and Call Centre activities and not in the business of investment means that the prime business of the assessee is of running BPO and Call Centres and as recorded by the Tribunal the entire funds were borrowed so as to expand the business activities of BPO and Call Centres in Canada by acquiring a Canadian company. Thus, the loan was taken for the purpose of business. This is a finding of fact which has not been shown to be perverse. The expansion of one's activities in Canada would require acquisition of a company by purchasing shares therein so as to expand the assessee's business. The object of the expenditure clearly is for the purpose of the business and, therefore, the interest incurred on the funds borrowed for investment in MC Canada has to be allowed as a deduction under section 36(1)(iii). So far as the finance expenditure is concerned, it would follow the allowing of interest expenditure. This expenditure is incurred in respect of the above loan taken for purpose of business and allowable under section 36(1)(iii). [Para 6]

## **CASES REFERRED TO**

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*CIT v. Srishti Securities (P.) Ltd.* [2009] 183 Taxman 159/[2010] 321 ITR 498 (Bom.) (para 6).

**Ashok Kotangale** for the Appellant. **J.D. Mistri**, Sr. Adv. and **Atul K. Jasani** for the Respondent.

## **ORDER**

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1. Income Tax Appeal No.867 of 2017- Not on Board. Mentioned. Upon mentioning taken on Board to be heard along with Income Tax Appeal No.778 of 2017 which is on Board as they arise from the common impugned order dated 25 August 2016 passed by Income Tax Appellate Tribunal, (Tribunal).
2. Mr.Kotangale learned counsel appearing in support of the Appeals seeks liberty to change the name of the Respondent to its present name i.e. Concentrix Services India Private Limited. Amendment as sought for allowed. Amendment to be carried out forthwith. Re-verification dispensed with.
3. These two appeals under section 260A of the Income Tax Act challenge the common order dated 25 August 2016 passed by the Tribunal. The common impugned order dated 25 August 2016 allowed the Respondent-assessee's two appeals relating to Assessment Year 2008-09 and 2009-10. Thus the two appeals.
4. The Revenue urges the following three identical questions of law in both appeals for our consideration:—
  - '1. Whether on facts and in the circumstances of the case and in law, the Tribunal was justified in directing the AO/TPO to adopt 0.5% as the ALP of the guarantee commission charges provided by the Respondent Co.; without appreciating that the TPO had determined the ALP taking into consideration entity, country specific, currency risks and also considering the leveraged position taken by the assessee company which had an impact on its working capital?
  2. Whether on facts and in the circumstances of the case and in law, the Tribunal was justified in its direction that the money advanced to the AE as share application money is not to be considered as loan, ignoring the fact that this money was being utilized as working capital and not deposited in an escrow account in cases where monies are received in cases of share application?
  3. Whether on facts and in the circumstances of the case and in law, the Tribunal was justified in directing the AO to delete the disallowance u/s 36(1)(iii) of the IT Act, 1961 without appreciating the fact that the acquisition of business by way of investing into shares of that company through either Special Purpose Vehicle or directly cannot be considered to be ordinary event of the business and therefore, cannot be termed as expenditure incurred for the purpose of assessee's business, which is providing IteS services?'

5. Regarding Question Nos.1 and 2.

- (a) Mr.Kotangale learned counsel appearing in support of the appeals very fairly states that both these questions stand concluded against Revenue and in favour of Respondent-assessee in the Respondent's own case by the order of this Court dated 4 September 2019 in ITXA No.303 of 2006 (*Principal Commissioner of Income Tax-10 Mumbai v. Couceutrix Services India Pvt. Ltd.* [formerly known as Minacs Pvt. Ltd.]). Both these questions on identical facts have been decided in favour of the Respondent-assessee.
- (b) It is not the case of the Revenue, that there is any distinction in facts and/or law in the subject Assessment years, which would make order dated 4 September 2019 in ITXA No.303 of 2006 inapplicable to this case.
- (c) In the above view, these two questions do not give rise to any substantial question of law. Thus not entertained.

#### 6. Regarding Question No.3.

- (a) The Respondent is engaged in the business of providing Information Technology enabled Services such as Call Centres, BPO services, etc. During the subject Assessment Year 2008-09 and 2009-10, the Respondent had claimed expenses on account of interest and finance expenses as an allowable expenditure under section 36(1)(iii) of the Act. The above interest and finance expenses (exchange rate fluctuation loss) is in connection with loans taken for DBS Bank for acquisition of a Company i.e. M/s Minacs Canada. However, the Assessing Officer disallowed the above interest and the finance expenses claimed under section 36(1)(iii) of the Act on the ground that it relate to acquisition of shares of foreign subsidiary and not related to the business of the Respondent.
- (b) Being aggrieved with the order of the Assessing Officer for both the years, the Respondent filed appeals to the Commissioner of Income-Tax (Appeals) (CIT(A)) who upheld the view of the Assessing Officer for Assessment Year 2008-09. However as far as Assessment Year 2009-10 is concerned the CIT(A) allowed the Respondent's appeal. This by holding that the expenditure of interest and finances on loan taken were in the nature of business expenditure and therefore allowable was deduction under section 36(1) (iii) of the Act.
- (c) Being aggrieved with the order of the CIT(A) both the Revenue as well as the Respondent-assessee filed appeals for the Assessment Year 2009-10 and 2008-09 respectively, before the Tribunal.
- (d) The Tribunal by the common impugned order disposed of both appeals as the issue is identical. It found on facts that the Respondent-assessee wanted to expand its business operations in North America and European countries. For the purpose of extension of its business in the above countries it had three ways available to it i.e. set up a branch in those countries or to form new companies in those countries or acquire a company operating in those countries in the similar line of business. It was the business decision of the Respondent-assessee to opt for the third method as indicated hereinabove and having taken that decision it set up a Special Purpose Vehicle in Canada only to acquire shares in M/s.Minacs Canada from its existing shareholders. This had to be done in view of regulatory restrictions of Canada which prohibited the Appellant from investing directly in an Canadian Company. The impugned order of the Tribunal found that acquisition of shares in M/s.Minacs Canada by the Respondent is for the purpose of its business. The impugned order of the Tribunal further records that the interest bearing funds were utilised for purchasing these shares of M/s.Minacs Canada through a Special Purpose Vehicle and interest was paid on the loan and loss and gain in view of the foreign exchange variations characterised as finance expenses. The interest paid on borrowed funds was allowed as a deduction under section 36(1)(iii) of the Act. This by the Tribunal placing reliance upon decision of this Court in the case of *CIT v. Srishti Securities (P.) Ltd.* [\[2009\] 183 Taxman 159/\[2010\] 321 ITR 498 \(Bom\)](#), wherein this Court has held that the interest paid on borrowed funds for the purpose of acquiring controlling interest in another company would be allowable business expenditure. So far as Finance expense is concerned, the Tribunal notes the fact that for the earlier Assessment Year namely 2007-08 the profit/gain made on account of foreign exchange variations on loan taken was allowed by the Assessing Officer. However when the same resulted in a loss the Assessing Officer sought to deny the same. This the Tribunal found went against principles of consistency and therefore held that the loss/expenditure on account of finance expenses was allowable. It was in

the aforesaid circumstances that the Tribunal allowed the appeal of the Respondent-assessee for the Assessment Year 2008-09 and dismissed the Revenue's appeal for the Assessment Year 2009-10.

- (e) Mr. Kotangale, learned counsel appearing in support of the Appeal states that the interest payment on the loan and finance expenditure on account of foreign exchange variations in the loan repayment could not have been allowed as business expenditure. This in view of the fact that the Respondent is not in the business of investment in shares but was in the business of Information Technology enabled Services, BPO and Call Centres.
- (f) We note that it is undisputed that the business of the Respondent-assessee is of running of BPO and Call Centres. Nor is it disputed that M/s.Minacs Canada is also in the business of Information Technology enabled Services i.e. BPO and Call Centre. It was the business decision of the Respondent to enhance/expand its activities and presence in the world market for that purpose had acquired controlling interest in the business of M/s.Minacs Canada which was in the same line of business as the Appellant. To make the above investment for the purpose of its business the loan was taken. Therefore the interest expenditure incurred on loans taken for investment in acquiring controlled interest in a Company which was in the same line of business as that of the Respondent would be allowable expenditure under section 36(1)(iii) of the Act. In *Srishti Securities (P.) Ltd, (supra)* the interest expenditure under section 36(1)(iii) of the Act had been disallowed by the Assessing Officer on the ground that the primary object of acquiring shares was only to acquire controlling interest in the Company. Thus not for purposes of business. This the Tribunal negated. Further in Appeal this Court has held that where an assessee claims deduction of interest paid on capital borrowed, all that an assessee has to show is that the borrowed funds were used for business purpose and if so then interest will have to be allowed as a deduction. The submission on behalf of the Revenue that the Petitioner is in the business of BPO and Call Centre activities and not in the business of investment means the prime business of the assessee is of running BPO and Call Centres and as recorded by the Tribunal the entire funds were borrowed so as to expand the business activities of BPO and Call Centres in Canada by acquiring a Canadian Company. Thus the loan was taken for the purpose of business. This is a finding of fact which has not been shown to be perverse. The expansion of ones activities in Canada would require acquisition of a Company by purchasing shares therein so as to expand the assessee's business. The object of the expenditure clearly is for the purpose of the business and therefore the interest incurred on the funds borrowed for investment in M/s.Minacs Canada has to be allowed as a deduction under section 36 (1)(iii) of the Act. So far as the finance expenditure is concerned, it would follow the allowing of interest expenditure. This expenditure is incurred in respect of the above loan taken for purpose of business and allowable u/s 36(1)(iii) of the Act. In fact, it was so allowed by the Revenue in Assessment Year 2007-08.
- (g) In the above view the question as proposed does not give rise to any substantial question of law as it is essentially a finding of fact and covered by decision of this Court in *Srishti Securities (supra)*. Thus not entertained.

7. Accordingly, Appeals are dismissed. No order as to costs.

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\*In favour of assessee.

†Arising out of order of ITAT, Mumbai in ITA Nos. 867/2017 and 778/2017, dated 25-8-2016.