

IN THE INCOME TAX APPELLATE TRIBUNAL
COCHIN BENCH, COCHIN
BEFORE S/SHRI CHANDRA POOJARI, AM & GEORGE GEORGE K., JM

I.T.A. Nos.409/Coch/2014 and 85 & 86/Coch/2016
Assessment Years : 2009-10, 2010-11 & 2011-12

M/s. Liberty Marketers, 44/356,Liberty Towers, Manapatti Parambu Road, Kaloor, Ernakulam, Kochi-682 017. [PAN:AABFL 6579Q]	Vs.	The Assistant Commissioner of Income-tax, Circle-2(2), Kochi.
(Assessee-Appellant)		(Revenue-Respondent)

Assessee by	Shri Anil D. Nair, Adv.
Revenue by	Shri A. Dhanaraj, Sr. DR

Date of hearing	02/04/2018
Date of pronouncement	03/04/2018

ORDER

Per Bench:

These appeals filed by the assessee are directed against different orders of the CIT(A)-II, Kochi and pertain to assessment years 2009-10, 2010-11 and 2011-12.

2. Since the issue involved in these appeals is common, hence they were heard together and are being disposed of by this consolidated order for the sake of convenience.

3. The only issue in these appeals is with regard to disallowance of portion of the interest paid on secured loans from banks as proportionate interest pertaining to personal drawings made by the partners.

4. Since the facts are common in all these appeals, we consider the facts as emanating from the appeal for the assessment year 2009-10. The Assessing Officer while making the assessment had gone into the details of drawings made by various partners from the firm and the secured loan taken by the assessee by bringing out the working of interest on debit balance and drawings in respect of three partners. Interest chargeable on their withdrawals was worked out by the Assessing Officer as:-

i) Shri Fisel	: Rs. 4,08,649/-
ii) Shri Siyaj	: Rs. 3,96,558/-
iii) Shri Zulfikar	: Rs.18,24,738/-
Total amount of interest chargeable	: Rs.26,29,945/-

4.1 This total interest of Rs.26,29,945/- was disallowed u/s. 36(1)(iii) by the Assessing Officer relying on the decision of Madras High Court in the case of Milapchand R. Shah vs. CIT (58 ITR 525) and Roopchand Chanbildass & Sons vs.

CIT (63 ITR 166) and that of Allahabad High Court in the case of Marolia & Sons vs. CIT (129 ITR 475). Similar disallowance was made for the assessment year 2010-11 at Rs.24,37,980/- and for 2011-12 at Rs.27,93,606/-.

5. According to the CIT(A), if any amounts are used for non business purposes by the assessee, the same are to be disallowed u/s 36(1)(iii). Since in this case the three partners have made these drawings from the partnership firm and these drawings have not been used for any business purposes, therefore according to the CIT(A), the provisions of section 36(1)(iii) are squarely applicable. The CIT(A) observed that the assessee tried to contend that while making these advances to the partners the assessee had enough credit in its books so as to allow interest free credit to its partners but since it was noticed from the detailed working made out by the assessing officer about the debit balance and drawings in respect of three partners that various amounts as brought out in the tables in the assessment order have been given to the partners, the assessee was asked to show that such payments were made from the surplus funds available with the assessee as contended in the submissions made.

5.1 In this connection, the CIT(A) observed that the assessee furnished a copy of its bank statement to show that the various payments were made from the credit balance received from sales etc., which were received just before making these advances to the partners. However, the CIT(A) did not justify the

explanation of the assessee as it was seen that the bank statement of assessee is a continuous over draft facility where balance on any particular day in the whole year in the bank statement was more than a 2 crores debit figure. Thus according to the CIT(A), even if a payment is received from the business transactions/sales, the same goes into the bank account and it only has the effect of reducing the over draft balance in the bank. Thus the CIT(A) observed that it was clear that if the bank balance of the assessee was a continuous debit balance then the assessee was making regular payment of interest on such debit balance to the bank and hence any payments made out of this bank statement has the character of interest being funds which was diverted to the partners of the assessee for non business purposes. According to the CIT(A), all the payments that was made to the partners were seen and they had gone from this bank account showing continuous debit balance. For the sake of record and clarity, the CIT(A) observed that for one entry made on 1.11.2008 to Shri Fisel of Rs.7,00,000/-, various entries in the bank on that day are as follows:

Date	Reference	Cheque No.	Debit	Credit	Balance
1 Nov2008	Outward clg	23943865	-	1,46,713.00	-2,66,55,446.20
1 Nov2008	Outward clg	23943890	-	64,454.00	-2,65,90,992.20
1 Nov 2008	Outward clg	23943920	-	20,668.00	-2,65,70,324.20
1 Nov 2008	Outward clg	23943958	-	10,00,000.00	-2,55,70,324.20
1 Nov 2008	Outward clg	23946744	-	15,000.00	-2,55,55,324.20
1 Nov 2008	Outward clg	23944301	-	19,386.00	-2,55,35,938.20
1 Nov 2008	FISEL	1303	7,00,000.00		-2,62,35,938.20

5.2 The CIT(A) observed that although assessee tried to explain that payment of Rs. 7,00,000/- was made from Rs. 10,00,000/- credit coming on the same day, but the fact remains that the credit of Rs. 10,00,000/- only had the effect of reducing overdraft facility of more than 2 crores, and hence for the payment of Rs.7,00,000/- to Shri Fisel, interest bearing funds was utilized. The CIT(A) found that it was exactly the same pattern that was repeated for all the payments to these partners. Thus according to the CIT(A) it was established that the payments to the partners have been made for non-business purposes from interest bearing funds. Hence, according to the CIT(A), the assessing officer was right in working out the interest on debit balances and total drawings in respect of these partners and making the disallowance u/s. (1)(iii) of the IT Act and confirmed the same.

5.3 Further, the CIT(A) noticed that in the additional ground of appeal, the assessee contended that even if any disallowance u/s 36(1)(iii) was made, this could only be made for the increase in advances during the year and not on the debit balance, in this regard, the assessee relied on the case law of CIT Vs Sridev Enterprises, 192 ITR 115(Kar). However, according to the CIT(A), it was seen that in that case such observation that disallowance could not be made for interest on debit balance was made in the light of the fact that there was no nexus that was shown that such payments were made from interest bearing funds in the earlier years. In the present case, the CIT(A) noticed that since the

payments to the partners were made from interest bearing funds, and such nexus was also evident from the bank statement filed, therefore the CIT(A) dismissed all the grounds of appeal filed by the assessee.

6. Against this the assessee is in appeal before us. The Ld. AR pleaded that the ratio of the judgments relied on by the Assessing Officer would not apply in the facts of the case as in those matters there were maximum funds both interest and non interest bearings. The Ld. AR objected to the finding of the Assessing Officer that as per the balance sheet, the assessee had substantial interest free funds being credit balance in respect of two partners, supply credit of Rs.6,46,40,000/- in the sundry creditors accounts and the profitability of the current year. It was submitted that the statement that interest free funds exceeded interest bearing funds in the relevant year was not controverted by the authorities below.

6.1 The Ld. AR relied on the judgments of the Supreme Court to contravene the disallowance:

- 1) S.A. Builders vs. CIT (288 ITR 1) (SC)
- 2) CIT vs. Hotel Savera (239 ITR 795) (Mad.)
- 3) Chanchal Katyal vs. CIT (298 ITR 182) (All)
- 4) CIT vs. Prem heavy Engineering Works (P) Ltd. (285 ITR 554) (All)
- 5) ONGC vs. DCIT (262 ITR 648) (Uttaranchal)
- 6) CIT vs. Raghuvir Sythetics Ltd. (36 Taxman.com 275) (Guj)
- 7) CIT vs. Reliance Utilities & Power Ltd. (178 Taxman 135) (Bom)

Therefore, by applying the ratios of the above mentioned judgments, it was submitted that since the assessee had common funds both interest bearing and non interest bearing and the same was found in one account, the withdrawals made for non business purpose were out of non interest bearing own funds.

6.2 Further the Ld. AR by way of additional grounds submitted that on similar facts, no disallowance was made in respect of this issue in earlier assessment years upto 2008-09. The ld. AR submitted that since no disallowance was made in respect of the debit balances of the partners in the earlier assessment years as it was utilizing the borrowed money, otherwise than for business purpose, the opening debit balance of the partners could not be considered during the current year and disallowance was to be limited to the increase in the partners debit balance of the current year only. The Ld. AR placed reliance on the judgment of the Karnataka High Court in the case of CIT vs. Sridev Enterprises (192 ITR 165).

7. On the other hand, the Ld. DR submitted that the assessee diverted interest bearing funds for non-business purpose by way of allowing withdrawals by the partners of the assessee-firm. Hence, interest expenditure is not wholly and exclusively laid out for the purpose of business. Accordingly, he supported the disallowance made by the Assessing Officer u/s. 36(1)(iii) of the Act and confirmation of the same by the CIT(A). He relied on the following judgments:

- i) Madhav Prasad Jatia vs. CIT (118 ITR 200 (SC))
- ii) CIT vs. V.I. Baby (254 ITR 248 (Ker.))
- iii) Somasundaram & Brothers vs. CIT (239 ITR 795) (Mds.)

7.1 The Ld. DR distinguished the judgments relied upon by the assessee. The Ld. DR submitted that the facts in the case of CIT vs. Hotel Savera (supra) are that the advance was made with assessee-firm's own funds and interest paid on borrowed capital was deductible. Similarly, according to the Ld. DR, the facts in the case of Chanchal Katyal vs. CIT (supra) is different since the assessee in that case had sufficient funds other than borrowed money. The facts in the case of CIT vs. Prem Heavy Engineering Works (P) Ltd. (supra), according to the Ld. DR are different as in that case, the assessee had sufficient interest free funds. Similarly, it was submitted that the facts in the case of ONGC vs. CIT are different since the issue in that case was reopening of the assessment u/s. 147 of the Act.

8. We have heard the rival submissions and perused the material on record. In this case, the partners of the assessee-firm had withdrawn amount from the assessee-firm only for personal purpose. The assessee has been paying interest on borrowed funds. The withdrawals made by the partners was not utilized for the purpose of business and the assessee-firm has not derived any business advantage from such withdrawals by the partners. The assessee-firm has not charged any interest on the withdrawals made by the partners by way of paying

interest on its borrowings. However, at the same time, the assessee has incurred interest expenditure on the borrowals made by the partners of the assessee-firm.

8.1 The main contention of the Ld. AR is that the assessee is having sufficient cash balance to meet the withdrawals made by the partners. In our opinion, if the cash balance is available, it should be meant for the business purpose of the assessee-firm and not for the personal purpose of the partners of the assessee-firm. The assessee with liquidity cannot claim that it could give such cash balance for the benefit of the partners of the assessee-firm. Such advance made by the partners has not been used for the business purpose but for the personal benefit of the respective partners. Had the assessee-firm used such cash balance for the business purpose or for payment of borrowals made by the partners of the assessee-firm, it could have saved interest expenditure.

8.2 Further, the Ld. AR made an argument that only the withdrawals of the present assessment years is to be considered for computation of interest expenditure and the earlier old balance of advance in the name of the partners which was carried forward from the earlier years cannot be considered. In our opinion, this argument of the assessee's Counsel has no merit as the assessee is paying interest on such carried forward opening balance and incurred interest expenditure on it. Therefore, the total advance outstanding in the name of the

partners is to be considered for computation of interest disallowance in the case of the assessee-firm. Accordingly, we do not find any infirmity in the orders of the lower authorities. This common ground for all the assessment years is dismissed.

9. In the result, the appeals of the assessee are dismissed.

Order pronounced in the open Court on this 03, April, 2018.

sd/-
(GEORGE GEORGE K.)
JUDICIAL MEMBER

sd/-
(CHANDRA POOJARI)
ACCOUNTANT MEMBER

Place:

Dated: 03 April, 2018

GJ

Copy to:

1. M/s. Liberty Marketers, 44/356, Liberty Towers, Manapatti Parambu Road, Kaloor, Ernakulam, Kochi-682 017.
2. The Assistant Commissioner of Income Tax, Circle-2(2), Kochi.
3. The Commissioner of Income-tax(Appeals)-II, Kochi
4. The Pr. Commissioner of Income-tax, Kochi
5. D.R., I.T.A.T., Cochin Bench, Cochin.
6. Guard File.

By Order

(ASSISTANT REGISTRAR)
I.T.A.T., Cochin