

**IN THE INCOME TAX APPELLATE TRIBUNAL
“SMC” BENCH, AHMEDABAD**

**BEFORE SHRI RAJPAL YADAV, JUDICIAL MEMBER And
SHRI WASEEM AHMED, ACCOUNTANT MEMBER**

आयकर अपील सं./ITA No. 1588/Ahd/2017

(निर्धारण वर्ष/Assessment Year : 2014-15)

Heaven Associates C/o.Akshat Heaven Opp.Sahjanand City, Kudasan Gandhinagar-382 421	बनाम/ Vs.	The ITO Ward-2 Gandhinagar
स्थायी लेखा सं./जीआइआर सं./PAN/GIR No. : AAGFH 8119 R		
(अपीलार्थी/Appellant)	..	(प्रत्यर्थी / Respondent)

अपीलार्थी ओर से/ Appellant by :	Shri Praveen Kumar, Sanu, AR
प्रत्यर्थी की ओर से/Respondent by:	Shri O.P. Pathak, Sr.DR

सुनवाई की तारीख/ Date of Hearing	28/03/2019
घोषणा की तारीख/Date of Pronouncement	27/05/2019

आदेश / ORDER

PER WASEEM AHMED, ACCOUNTANT MEMBER:

The captioned appeal has been filed at the instance of the Assessee against the order of the Commissioner of Income Tax (Appeals)–Gandhinagar, Ahmedabad [CIT(A) in short] vide appeal no.CIT(A)/GNR/82/2016-17 dated 17/04/2017 arising in the assessment order passed under s.143(3) of the Income Tax Act, 1961(hereinafter referred to as "the Act") dated 28/12/2016 relevant to Assessment Year (AY) 2013-14.

2. The assessee has raised the following grounds of appeal:-

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1. *That the learned CIT(A), Gandhinagar has erred in law and on the facts in passing appellate order dt.17/04/2017 and in partly allowing the appeal of appellant.*
2. *That the learned CIT(A) has erred and made observations (Para 4.3, pg.5) that the appellant has utilized higher interest bearing loan for earning lower interest, the learned CIT(A) has also state that the appellant should not have got disbursed loan from Bank of Baroda when it was not in need of any fund. It is pertinent to mention here that the terms of sanction letter of Bank are not gone through by the learned CIT(A) and by the AO, the terms as contained in sanction letter mentions various formalities to be done before disbursement of progress payments. The time frame between the formalities to be made for disbursement and the disbursement of loan amount sometimes took 30-45 days. Thus it was prudent business to get the disbursement from business though not required instantly in the business affairs. Thus appeal is made to consider the disbursement of loan as a prudence business.*
3. *The learned CIT(A) has rightly mentioned that the disallowance of interest expenses in current year would result into notional interest income, which is not permissible. Thus, the disallowance made by the AO in the current year to the extent of Rs.11,34,689/- after considering order u/s.154 is deleted. Further the Learned CIT(A) has grossly erred in directing the AO to reduce the closing WDV on the basis of progress report submitted by the appellant. Further, the Learned CIT(A) has wrongly mentioned that – “appellant is claiming that funds were idle hence it given interest free advances”, nowhere in submissions made before the learned CIT(A), appellant has mentioned this. Thus appeal is made to delete the direction by the learned CIT(A) to the AO to reduce the closing WIP with the amount of interest difference.*
4. *The CIT(A) has grossly erred in considering that there is diversion of business funds for non-business purpose. The CIT(A) has not considered the submission (available on record,*

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pg. 27-30 of paper book submitted to CIT(A) made before the AO vide dt. 23/12/2016 wherein appellant has justified that – “to save on cost of interest we have advanced the amounts available idle with the firm at 12% pa and thus saved on interest cost.” Thus the clear intention was to save interest cost and not to divert the funds. Thus the observations of learned CIT(A) that the business funds were diverted are bad in law and in the facts.

5. The appellant craves leave to add, alter/amend withdraw/modify any of the above grounds till the appeal is finally heard and decided.

3. The interconnected issue raised by the assessee is that the Ld. CIT (A) erred in confirming the addition in part made by the AO on account of diversion of funds for a non-business purpose.

4. The facts of the case are that the assessee is a partnership firm and engaged in the business of construction of residential and commercial units and sales thereof. The assessee advanced the loan to the sons and close relatives of the partner on interest at the rate of 12%. The assessee in support of its claim submits the ledger accounts of the borrower before the AO.

The assessee also claimed that it had received the loan from Bank of Baroda on interest at the rate of 15.10%. As such, the assessee to reduce the cost of interest on the bank borrowing provided advances which were idle with it to its relatives at the rate of interest of 12%.

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However, the AO on perusal of the audit report observed that the assessee had shown interest income of Rs. 4,96,177/- while on the other hand, it claimed interest expenses of Rs. 2,59,88,220/-.

The AO further observed that the assessee was not showing the interest income received on such advances in its books of account.

The AO also observed that the assessee received loan amounting to Rs. 33,00,00,000/- from Bank of Baroda at a rate of interest of 15.10%. Therefore the AO was of the view that the advances given to the sons and close relatives of the partner were out of the bank borrowings. Thus the AO disregarded the contention of the assessee and calculated the interest on such advances at the rate of 15.10% as under.

<i>“Sr.No.</i>	<i>Name</i>	<i>Interest worked Out by ‘A’ @12%</i>	<i>Interest worked @15.10%</i>
<i>1.</i>	<i>Darshan Baldev Patel</i>	<i>20,24,894</i>	<i>12,89,965</i>
<i>2.</i>	<i>Ramesh D.Patel</i>	<i>8,04,493</i>	<i>10,12,320</i>
<i>3.</i>	<i>Ajay P.Thadhani</i>	<i>20,52,526</i>	<i>25,82,276</i>
<i>4.</i>	<i>Devang Baldevbhai Patel</i>	<i>2,58,904</i>	<u><i>3,90,945</i></u>
	<i>Total interest disallowed</i>		<i>52,75,506</i>
	<i>And added to total income as no such Interest alleged to have been Charged is reflected in the audited Accounts.”</i>		

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The AO accordingly added the sum of Rs. 52,75,506/- to the total income of the assessee.

The aggrieved assessee preferred an appeal before the Ld. CIT (A).

5. The assessee before the Id. CIT(A) submitted that the interest expenses were shown as part of the stock in trade and accordingly the same was credited as closing stock in trade. Thus in the result, there was no effect on the profit of the firm.

The assessee also claimed that the AO made the apparent mistake while passing the assessment order under section 143(3) of the Act. Therefore it has requested through an e-mail dated 31/12/2016 and tapal dated 02/01/2017 to rectify the order under section 154 of the Act.

However, the Ld. CIT (A) observed that advances given to the relatives and sons against the loan received from Bank of Baroda were undisputed facts. The disputed facts are that the assessee paid interest at the rate of 15.10% on the said loan while on the other hand, it charged 12% on the said advances. As such the assessee already declared interest income of Rs. 41,40,817/- in its P&L account, so the addition amount reduces amounting to Rs. 11,34,689/- under section 154 of the Act vide order dated 24/01/2017.

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The Ld. CIT (A) also observed that the assessee did not require the loan as it had sufficient balance in the form of capital which was introduced by its partner.

Being aggrieved by the order of the Id. CIT(A), the assessee is in appeal before us.

6. The Id. AR before us filed a paper book running from pages 1 to 111 and submitted that the Ld.AO at the time of framing assessment order was in illusionary mindset that assessee firm has given interest free advances to the family member of the partners out of borrowed term loan from banks.

In this regard, it is duly submitted that assessee in its submission never said that it has given advances out of borrowed funds (Term Loan) from banks. Assessee has claimed since beginning that firm has given advances out of its own funds (ie. Ideal funds), which is misinterpreted by the Ld. AO and assumed that advances were made out of borrowed funds as free of cost.

Further, from balance sheet of the appellant it amply clear that appellant firm has enough own funds of Rs.15,09,83,384/- during the relevant year to make advance of Rs.7,74,74,750/-.

Judicial pronouncements

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In support of the contention of the firm, appellant has placed reliance on various judicial pronouncements of the courts which are in favour of the Assessee.

Assessee places reliance on the decision of the Hon'ble jurisdictional Gujarat High Court in the case of Gujarat Narmada Valley Fertilizers Co.Ltd. Vs. ACIT [42 Taxmann 579 (Gujarat-HC) (2004)], wherein it was held that when there were sufficient funds available with the assessee-company and out of which loans and advances to associate companies could be made. Assessing Officer was not justified to disallow claim of interest on borrowed funds. The full citation of the aforesaid decision is given below for your Honours' read reference (Page No.2-4 Paper Book II).

In support of above contention, the assessee further relies on following judicial pronouncements:-

- Raghuvir Synthetics Ltd. vs. CIT [36 Taxmann 275 (Gujarat-HC) (2013)]
- Munjal Sales Corporation v. CIT [298 ITR 298/Taxmann 43(SC)(2008)]
- Sunil Goel v. Asst.CIT
[118 TTJ (Del) 415, 422-23]
- Naresh Fabrics vs. ITO
[75 TTJ (Jodh) 386, 392-92]

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Accordingly, from above various citations of the courts in favour of the assessee, it is amply clear that assessee can give loans & advances out of own funds, and there should be no disallowance of interest expenses on borrowed funds.

Most of the advances has been given before the Term loan released by bank ie, on or before 19th August, 2013 which clearly shows that there is no nexus between advances & Term Loans.

Judicial pronouncements

In support of the above contention of the firm, appellant has placed reliance on various judicial pronouncements of the courts which are in favour of the Assessee.

The assessee also relies on the ruling of the Hon'ble jurisdictional Gujarat High Court in the case of Rajendra Brothers vs . CIT [52 Taxmann 334, (Gujarat-HC) (2004)], where it was held that there was no material on record indicating that there was diversion of interest bearing funds as interest free advances, assessee's claim for deduction under section 36(1)(iii) was to be allowed, full citation of the aforesaid decision is given below for your Honours' ready reference.

In support of above contention, the assessee, further relies on the ruling of the G.R. Agencies v. ITO (2003) 79 TTJ (Luck) 416, where it was held that most of the advances are prior to the borrowings and, therefore, it cannot be said that borrowed funds have been diverted to interest-free

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advances, full citation of the aforesaid decision is given below for your Honours' ready reference.

Relating to the above citation of the courts with our case, appellant has made most of advances before disbursement of Term loan ie, before 19th August-2013. Hence there is no nexus between the advances given with borrowed funds (Term Loans).

7. On the other hand the Id. DR before us vehemently supported the order of the authorities below.

8. We have heard the rival contentions of both the parties and perused the materials available on record. The assessee in the instant case has borrowed money from the bank on interest at the rate of 15.10% whereas it has given advances to the relatives of the partners of the firm on interest at the rate of 12% only. Thus the AO was of the view that the assessee has diverted interest-bearing fund at a lower rate of interest. Accordingly, the AO worked out the amount of interest for 11,34,689/- in the order rectified under section 154 of the Act vide order dated 24/01/2017 being the amount attributable to the amount advanced at a lower rate of interest. The learned CIT (A) subsequently confirmed the order of the AO.

At the outset, we note that owned fund of the assessee as on 31st March 2013 and 31st March 2014 stands at ₹9,20,43,295.00 and 15,09,83,383.00 which is more than the amount of advances of ₹7,66,40,811 given at a

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lower rate of interest. The details of the own fund and the amount of impugned advances are not in dispute. Therefore a presumption can be drawn that the assessee has advanced the money to the relatives of the partners out of its fund. In holding so, we find support and guidance from the judgment of Hon'ble Bombay High Court in the case of *Reliance Utilities and Power Ltd.* reported in 313 ITR 340 wherein it was held as under:-

“The principle therefore would be that if there are funds available both interest-free and overdraft and/or loans taken, then a presumption would arise that investments would be out of the interest-free fund generated or available with the company, if the interest-free funds were sufficient to meet the investments. In this case this presumption is established considering the finding of fact both by the CIT(A) and Tribunal”.

Similarly, we also rely on the judgment of the Hon'ble Bombay High Court in the case of *CIT vs. HDFC Bank Ltd* reported in 366 ITR 505 (Bom). The relevant extract of the order is reproduced below:-

“Where assessee's capital, profit reserves, surplus and current account deposits were higher than the investment in tax-free securities, it would have to be presumed that investment made by the Assessee would be out of the interest-free funds available with Assessee and no disallowance was warranted u/s 14A.”

Similarly, we also find support from the judgment of Hon'ble Gujarat High Court in the case of *UTI Bank Ltd.* reported in 32 Taxmann.com 370 where the headnote reads as under :

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“If there are sufficient interest free funds to meet tax free investments, they are presumed to be made from interest free funds and not loaned funds and no disallowance can be made under section 14A”.

In view of the above proposition, we hold that no disallowance of interest expense claimed by the assessee can be made on account of investments as discussed above. Hence, we reverse the order of the authorities below. The AO is directed to delete the addition made by him. Hence the ground of appeal of the assessee is allowed.

9. In the result, the appeal of the assessee is allowed.

This Order pronounced in Open Court on	27/05/2019
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Sd/-
(RAJPAL YADAV)
JUDICIAL MEMBER

Sd/-
(WASEEM AHMED)
ACCOUNTANT MEMBER

Ahmedabad; Dated 27/05/2019

टी.सी.नायर, व.नि.स./T.C. NAIR, Sr. PS

आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent.
3. संबंधित आयकर आयुक्त / Concerned CIT
4. आयकर आयुक्त(अपील) / The CIT(A)-Gandhinagar, Ahmedabad
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, अहमदाबाद / DR, ITAT, Ahmedabad
6. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER.

सत्यापित प्रति //True Copy//

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