

IN THE INCOME TAX APPELLATE TRIBUNAL
'B' BENCH : BANGALORE
BEFORE SHRI CHANDRA POOJARI , ACCOUNTANT MEMBER
AND
SMT. BEENA PILLAI, JUDICIAL MEMBER

ITA No.2308/BANG/2019
Assessment Year : 2014 - 15

Mittal Clothing Company, 102, 3 rd Cross, 3 rd Main, 2 nd Stage, Industrial Suburb, Yeshwanthpur, Bengaluru-560 022.	Vs.	The Asst. Commissioner of Income Tax, Circle-6(2)(1), Bengaluru.
PAN - AABFM 6725 H		
APPELLANT		RESPONDENT

Appellant by	:	Shri V Srinivasan, Advocate
Respondent by	:	Shri Priyadarshi Mishra, JCIT (DR)

Date of Hearing	:	26-11-2020
Date of Pronouncement	:	27-11-2020

ORDER

PER BEENA PILLAI, JUDICIAL MEMBER

Present appeal has been filed by assessee against order dated 27/08/2019 passed by Ld.CIT(A)-6, Bangalore for assessment year 2014-15 on following grounds of appeal:

"1. The impugned order passed by the learned Commissioner of Income Tax (Appeals) under section 250 of the Income Tax Act, 1961 to the extent which is against the Appellant is opposed to law, weight of evidence, probabilities, facts and circumstances of the case.

2. The learned Commissioner of Income Tax (Appeals) erred in law and in facts in her order by rejecting the Appellant's contention that there could no interest disallowance when the Appellant has own interest free funds and the same far exceeds the amount advanced to sister concern and when such advance was made in the earlier assessment years and failed

note that when two reasonable constructions are possible, the one that is favourable to the assessee is to be preferred, in as much as failed to appreciate the merits of the case.

3. The order of the learned assessing officer in so far it is prejudicial to the interest of the appellant is bad, erroneous in law and contrary to the facts and circumstances of the case and the

4. Ld. Commissioner(Appeals) erred in upholding the same.

4. The learned Assessing Officer is erred in law and on facts in making interest disallowance of Rs. 27,59,642/- and the Ld. Commissioner(Appeals) erred in upholding the same.

5. The Appellant submits that each of the above grounds are mutually exclusive and without prejudice to one another.

6. The Appellant craves leave to add, alter, amend, vary, omit or substitute any of the aforesaid grounds of objection at any time before or at the time of hearing before the Honourable Income Tax Appellate Tribunal (Tribunal), so as to enable the Hon'ble Tribunal to decide on the appeal in accordance with the law.

7. For these and other grounds that may be urged at the time of hearing of appeal, the Appellant prays that the appeal may be allowed for the advancement of substantial cause of justice and equity.”

Brief facts of the case are as under:

2. Assessee is a firm and filed its return of income for year under consideration on 01/10/2014 declaring total income of Rs.36,79,870/-. The case was selected for scrutiny and notice under section 143(2) and 142(1) was issued to assessee. In response to statutory notices, representative of assessee appeared before Ld.AO and filed requisite details as called for.

During assessment proceedings, Ld.AO noted that assessee had advanced certain funds amounting to Rs.1,68,51,000/- to M/s.G.N.Mittal Investments Pvt Ltd., without any interest. The Ld.AO noted that assessee had taken loans from banks to the extent of Rs.6,41,79,43/- and was paying interest of Rs.1,05,75,139/- which was claimed as expenditure.

Ld.AO was of the opinion that assessee diverted interest-bearing funds to M/s.G.N.Mittal Investments Pvt.Ltd., and therefore

disallowed proportionate interest amounting to Rs.27,59,642/- as an amount not related to business expenditure.

3. Aggrieved by addition, assessee preferred appeal before the Ld.CIT(A).

4. Ld.CIT(A) after considering the submissions by assessee observed as under:

5. I have carefully considered the facts of the case, the grounds of appeal and the statement of facts and the written submission filed. The sole issue raised in the grounds of appeal is that the addition of Rs.27,59,642/- out of interest on bank loan was incorrect. The appellants contention is that it had sufficient own funds in the partners capital account in order to make the investment in the related party i.e. C.N - Mittal Investments Pvt. Ltd. Perusal of the balance sheet of the appellant shows an amount of Rs. 11 5, 10,866/ - in the partners' capital account. The balance outstanding in hands of G.N. Mittal Investment Pvt. Ltd. as on 31/03/2013 was Rs. 1,68,51,000/-. While the record shows that there were no fresh investment in G.N. Mittal Investment Pvt. Ltd. during the year under appeal and that there was repayment of Rs.1,03,000/- by the party during this period, the fact remains that interest was collected from the related party whereas huge interest of Rs. 1,05,75,139/ - was paid to the banks.. In the financial statements, the amount t is shown as a loan to G.N. Investments P. Lid. The appellant has not established the business expediency of this transaction with the related party nor has it explained as to why the loan was given as an interest-free one. In the case of CIT vs Abhishek Industries 205 CTR P H 304, the Hon'ble Punjab and Haryana High Court had held as follows: "Section -36(iii) of the Act provides for deductions of interest on the loans raised for business purposes. Once the assessee claims any such deduction in the books of accounts, the onus will be on the assessee to satisfy the Assessing Officer that whatever loans were raised by the assessee, the same were used for business purposes. If in the process of exan2ination of genuineness of such a deduction, it transpires that the assessee had advanced certain funds to sister concerns or an' other persons without any interest., there would be very heavy onus on the assessee to be discharged before the Assessing Officer to the effect that in spite of pending term loans and working capital loans on which the assessee is incurring liability to pay interest, still there was justification to advance loans to sister concerns for non-business purposes without any interest and accordingly, the assessee should be allowed deduction of interest being paid on the loans raised by it to that extent. In our view, even the plea of nexus of loans raised by the assessee with the funds

advanced to the sister concerns on interest free basis, may he it is pleaded to the out of sale proceeds or share capital or different account cannot be accepted. Entire money in a business entity comes in a common kitty. The monies received as share capital, as term loan; as working capital loan., as sale proceeds etc. do not have any different colour. Whatever are the receipts in the business, that have the colour of business receipts and have no separate identification. Sources has no concern whatsoever. The only thing sufficient to disallow the interest paid on the borrowing to the extent the amount is lent to sister concern without carrying any interest for non-business purpose would be that the assessee has some loans or other interest bearing debts to be repaid. In case the assessee had some surplus amount which, according to it, could not be repaid prematurely to any financial institution, still the same is either required to be circulated and utilised for the Put pose of business or to be invested in a manner in which it generates income and not that it is diverted towards sister concern free of interest. This would result in not presenting true and correct picture of the accounts of the assessee as at the cost being incurred by the assessee, the sister concern would be enjoying the benefits thereof. it cannot possibly be held that the funds to the extent diverted to sister concerns or other persons free of interest were required by the assessee for the purpose of its business and loans to that extent were required to be raised. We do not subscribe to the theory of direct nexus of the funds between borrowings of the funds and diversion thereof for non business purposes. Rather, there should be nexus of use of borrowed funds for the purpose of business to claim deduction under Section 36(1)(iii) of the Act. That being the position, there is no escape from the finding that interest being paid by the assessee to the extent the amounts are diverted to sister concern on interest free basis are to be disallowed.

13. If the plea of the assessee is accepted that the interest free advances made to the sister concerns for non-business purposes was out of its own funds in the form of capital introduced in business, that again will show a camouflage by the assessee as at the time of raising of loan, the assessee will show the figures of capital introduced by it as a margin for loans being raised and after the loans are raised, when substantial amount is diverted to sister concerns for non-business purposes without interest, a plea is sought to be raised that the amount advanced was out of its capital, which in fact stood exhausted in setting up of the unit. Such a plea may be acceptable at a stage when no loans had been raised by the assessee at the time of disbursement of funds. This would depend on facts of each case. Section 106 of the Indian Evidence Act or the principles analogous thereto places the burden in respect thereof upon the assessee, as the facts are within its special knowledge. However, a presumption may be raised in a given case as to why an assessee who for the purpose of running its business is required to borrow money from

banks and other financial institutions would be giving loan to its subsidiary companies and that too when it pays a heavy interest to its lenders, it would claim no or little interest from its subsidiaries.

An assessee with liquidity cannot claim that it can give interest free advances to the partners and others and then borrow funds from the bank on interest for business purposes. Such borrowings will not be for business purposes, but for supplementing the cash diverted by the assessee without any benefit to it. Therefore, so long as the assessee is not the beneficiary of the investments made by the partners, their relatives and the sister concerns, and so long as the advances are interest free, the Assessing Officer is perfectly justified in disallowing the interest in proportion to the advances made.

Once it is borne out from the record that the assessee had borrowed certain funds on which liability to pay tax is being incurred and on the other hand, certain amounts had been advanced to sister concerns or others without carrying any interest and without any business purpose, the interest to the extent the advance had been made without carrying any interest is to be disallowed under Section 36(1)(iii) of the Act. Such borrowings to that extent cannot possibly be held for the purpose of business but for supplementing the cash diverted without deriving any benefit out of it. Accordingly, the assessee will not be entitled to claim deduction of the interest on the borrowings to the extent those are diverted to sister concerns or other persons without interest.

The facts of the appellants case are similar to those of Abhishek Industries supra. In light of the legal position enunciated in the above decision, the AO's action in disallowing proportionate interest of Rs. 27,59,642/- is upheld. The grounds of appeal raised are dismissed."

5. Ld.CIT(A) relying on decision of Hon'ble Punjab and Haryana High Court in case of *CIT vs Abhishek Industries* reported in 286 ITR 1 upheld the addition made by Ld.AO.

6. Aggrieved by order of Ld.CIT(A) assessee is in appeal before us now.

7. The only issue raised by assessee is in respect of disallowance of interest under section 36(iii) of the Act.

8. Ld.AR submitted that, assessee had interest-free funds in the following manner:

Particulars	Amount (Rs.)	Amount (Rs.)
Partners capital	11,88,80,067/-	
Reserves and surplus	16,46,000/-	
Non-interest bearing unsecured funds	10,45,10,000/-	22,50,36,067/-
Amount advanced to M/s.G.N.Mittal Investment Pvt.Ltd.		1,68,51,000/-

9. Placing reliance on page 20 of paper book, Ld.AR submitted that, assessee had advanced funds to its sister concern in the earlier assessment year amounting to Rs.1,68,51,000/- and the balance outstanding as on 31/03/2014 was Rs.1,67,48,000/-. He placed reliance on the decision of *Hon'ble Bombay High Court* in case of *Reliance Utilities and Power Ltd* is reported in *313 ITR 340*.

10. On the contrary Ld.SR.DR placed reliance on orders passed by authorities below.

11. We have perused submissions advanced by both sides in light of records placed before us.

12. We note that assessee has sufficient funds in the form of partners capital and reserves and surplus as its own funds. It is also noted by us that the funds were advanced to the sister concern in the preceding assessment year and it reduced in the current year. The Ld.AR filed before us, decision of *Hon'ble Karnataka High Court* in case of *CIT vs M/s.Brindavan Beverages Pvt Ltd* in *ITA No.67 of 2015*, wherein, *Hon'ble court* by order dated 26/10/2016 has observed that decision relied upon by

Ld.CIT(A) of *Hon'ble Punjab and Haryana High Court*, has been reversed by *Hon'ble Supreme Court* in case of *Munilal Sales Corporation vs CIT* reported in decision relied upon by Ld.CIT(A) of *Hon'ble Punjab and Haryana High Court*, the same has been reversed by *Hon'ble Supreme Court* in case of *Munilal sales Corporation vs CIT* reported in 298 ITR 288.

13. Respectfully following the above view, the view taken by Ld.CIT(A) deserves to be reversed. We direct Ld.AO to delete the disallowance of interest made under section 36(iii) of the Act amounting to Rs.27,59,642/-.

Accordingly grounds raised by assessee stands allowed.

In the result appeal filed by assessee stands allowed.

Order pronounced in the open court on 27th Nov, 2020

Sd/-
(CHANDRA POOJARI)
(BEENA PILLAI)
Accountant Member
Judicial Member

Sd/-

Bangalore,
Dated, the 27th Nov, 2020.
/Vms/

Copy to:

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

By order

Assistant Registrar, ITAT, Bangalore

		Date	Initial	
1.	Draft dictated on	On Dragon		Sr.PS
2.	Draft placed before author	-11-2020		Sr.PS
3.	Draft proposed & placed before the second member	-11-2020		JM/AM
4.	Draft discussed/approved by Second Member.	-11-2020		JM/AM
5.	Approved Draft comes to the Sr.PS/PS	-11-2020		Sr.PS/PS
6.	Kept for pronouncement on	-11-2020		Sr.PS
7.	Date of uploading the order on Website	-11-2020		Sr.PS
8.	If not uploaded, furnish the reason	--		Sr.PS
9.	File sent to the Bench Clerk	-11-2020		Sr.PS
10.	Date on which file goes to the AR			
11.	Date on which file goes to the Head Clerk.			
12.	Date of dispatch of Order.			
13.	Draft dictation sheets are attached	No		Sr.PS

