

**INCOME TAX APPELLATE TRIBUNAL
MUMBAI 'SMC' BENCH, MUMBAI**

[Coram: Pramod Kumar (Vice President)]

ITA No. 4479/Mum/2019
Assessment Year: 2015-16

Ashok Raitlal Miyani

1201, Shatrunjay Apartment, Neelkanth Valley,
7th Rajawadi Road, Ghatkopar (E)
Mumbai 400077 [PAN: AAOPM0711C]

..... Appellant

Vs.

**Income Tax Officer 27 (1) (2)
Mumbai.**

.....Respondent

Appearances:

Mehul Shah for the appellant

Nijaykumar Menon for the respondent

Date of concluding the hearing: : May 10, 2021

Date of pronouncement : August 06, 2021

O R D E R

Per Pramod Kumar, VP:

1. By way of this appeal, the assessee-appellant has challenged the correctness of the order dated 20th May 2019, passed by the learned CIT(A) in the matter of assessment u/s. 143(3) of the Income Tax Act, 1961 for the assessment year 2015-16.

2. Grievances raised by the assessee, which are interconnected and will be taken up together, are as follows:-

1. On the facts, and in circumstances of the case, and in law, learned Commissioner of Income-tax (Appeal) erred in upholding action of the Assessing Officer in proportionately disallowing interest on borrowing amounting to Rs.1,962,710 invoked alleging that entire borrowed funds were not utilized for the purpose of investment in partnership concerns without appreciating that the appellant was partner in three different concerns, and capital contribution in these concerns was larger than the amount of borrowed funds.

2. On the facts, and in circumstances of the case, and in law, learned Commissioner of Income-tax (Appeal) and the Assessing Officer erred in not appreciating that the flats allotted upon consent terms filed following to the Arbitration Award constituted business assets of the Appellant which qualified for deduction of interest on borrowed funds.

3. Briefly stated, relevant material facts are like this. The assessee before us is an individual and his case was selected for limited scrutiny for the purpose of examining “deductions from income from other sources and purchase of property”. In the course of resultant scrutiny assessment, proceedings, the Assessing Officer disallowed interest deduction of Rs. 19,62,710/- by observing as follows:-

4) Disallowance of interest u/s. 57 (iii):

On perusal of return of income, it is seen that the assessee has claimed interest expenses of Rs.30,92,631/- against interest income of Rs.1,24,229/-, LIC pension of Rs.58,044. Thus the assessee has declared loss under the income from other sources at Rs.29,10,358/-. On further perusal of the business income it is seen that the assessee is deriving interest on his capital with partnership firm of M/s. AM Developers and M/s Manmantra Infra Com LLP. It has been further observed that the assessee has borrowed fund to the tune of Rs.5,12,10,068/-. However the assessee's capital in the partnership firm which inclusive of current year's interest amounts to Rs.3,41,47,071/-. In view of this during the course of assessment proceedings vide notice u/s. 142(1) dated 13/11/2017, it was brought to the notice of the assessee that his capital in the partnership firm of M/s. AM Developers and M/s. Manmantra Infracom LLP is only Rs.3,41,47,071/- and the borrowed unsecured loans amounts to Rs.5,12,10,068/- and, therefore, it cannot be said the entire borrowed funds have been utilised for the purpose earning interest. Therefore, the assessee was asked to explain as to why the proportionate interest attributable to the borrowed funds which has not been utilised for earning the interest should not be disallowed. In response to this the assessee vide letter dated 01/12/2017, submitted that the assessee has claimed set off of interest paid of Rs.30,92,631/- u/s. 71 of the Income tax Act against various income offered to tax under head of Income from Profits and gains of business and income from other sources etc. It has been further submitted that the loss under the income from other sources is allowable against profits and gains of business and income from house property and other sources as per the provisions of section 71(1) of the Income tax Act. The assessee's above submissions have been considered. The issue involved in this case is the allowability of interest expenses u/s. 57(ii) and not the set off of the loss from income from other sources against the income of profits and gains of business. During the course of assessment proceedings it has been submitted that the assessee was partner in M/s. Avi Housing Realtors and due to certain dispute in the project the work of the firm to stand still and matter was referred to arbitration before the sole arbitrator Mr. A.V. Potdr, Retd., Judge and the award was given by him in terms of concerned term. As per the terms of the award he has been paid an amount of Rs.4,23,61,576/- on 09/12/2013 and the balance capital was repaid to him by way of right in the flat bearing No. 1004/1101 and 1102. The total cost of the three flats amounts to Rs. 3,25,00,000/-. It is a contention of the assessee that the borrowed funds have been

utilised for the purpose of introduction of capital in the partnership firm of M/s. Avi Housing Realtors. Since the entire capital have been repaid to the assessee during the F.Y 2013-14 by way of payment of cheque of Rs.4,23,61,576/- and allotment of the flat against the capital of Rs.3,25,00,000/- and there is no capital balance is with M/s. Avi Housing Realtors as on 09/05/2014. Therefore, it is clear that the borrowed funds to the extent of Rs.3,25,00,000/- has not been utilised for the purpose of any interest income. It has been further informed by the assessee that the project in which the flat was allotted to the assessee is not yet completed and the assessee has not given the possession of the property. In view of this the interest attributable to the three flats should be capitalised and added to the cost of the flat, therefore, interest on the borrowed funds of Rs.3,25,00,000/- has not been utilised for the purpose of investment in partnership firm from where the assessee has received the interest income. Accordingly the proportionate interest attributable for the cost of three flats is disallowed u/s. 57(iii) and added to the total income of the assessee. The disallowance is computed as under:

<i>Total borrowed funds</i>	<i>Rs. 5,12,10,068/-</i>
<i>Cost of the three flats</i>	<i>Rs. 3,25,00,000/-</i>
<i>Interest paid on borrowed funds</i>	<i>Rs. 30,92,631/-</i>
<i>Therefore, the disallowance u/s. 57(iii)</i>	<i>Rs.3,25,00,000/- X 30,92,631 = Rs 19,62,710/-</i>
	<i>Rs. 5,12,10,068</i>

4. Aggrieved assessee carried the matter in appeal before the CIT(A) and pointed out that, under the arbitration settlement with the partners, the assessee had to accept rights in respect of three flats in an under construction project at a somewhat high value of Rs. 3.25 crores. This right, according to the assessee, was a part and parcel of his investment in the firm. Accordingly, he should not be declined interest on borrowings to that extent. These submissions, as also assessee's other submissions, were rejected by the CIT(A). Dismissing the arguments raised by the assessee, learned CIT(A) observed as follows:-

5. The facts of the case are very clear. The issue at hand is the allowability of interest u/s 57(iii) of the I. T. Act. Before section 57 can apply, the following general conditions must be met:

i) The expenditure must have been incurred solely and exclusively for the purpose of making or earning such income.

ii) The expenditure should not be in the nature of a capital expenditure

(iii) The amount in question should not be in the nature of personal expenses of the assessee. (Section 58(1) of the Act)

iv) The expenditure should be incurred in the accounting year.

v) There must be a clear nexus between the expenditure incurred and the income sought to be earned.

vi) *The expenditure which can be allowed is only of the nature specified in section 57 of the Act.*

Section 57(ii) declares that any other revenue expenditure laid out or expended wholly and exclusively for the purpose of making or earning such income is to be allowed as a deduction. However there is a crucial difference between section 37(1) and section 57 of the Act. Section 37(1) simply permits deduction of revenue expenses and non-personal expenses which have been laid out or expended wholly and exclusively for the purposes of the business or profession of the assessee. The scope of allowability of the expenses under section 37(1) of the Act is very wide and all expenses incurred for the purposes of the business or profession are to be allowed. In contrast, under section 57 of the Act the allowable expenses are only those which are laid out or expended for the purpose of making or earning such income only. Thus the scope of section 57 is confined to the allowability of expenses relating to earning of the particular income only, In the case law of Seth R. Dalmia v. CIT [1977] 110 TTR 644 (SC) it was held that the dominant purpose of the expenditure incurred must be to earn income. The connection between the expenditure and the earning of income need not be direct, even an indirect connection could prove the nexus between the expenditure incurred and the income. It is also to be seen that the 'purpose' contemplated by section 57(iii) points to a precise and specific object of making or earning income. This is not to be confused with 'motive'. The motive with which the expenditure is incurred is irrelevant. The purpose of making or earning this income must be the sole purpose for which the expenditure is incurred. If there is a mixed purpose, it is not possible to allow the deduction.

5.1 If the facts of the case are seen from the legal perspective, it is noted that the assessee has been paying interest on borrowed sums of Rs. 5.12 Crores whereas his capital in the partnership Firms was only Rs. 3.41 Crores. This immediately indicates that the borrowed funds have been used elsewhere. The assessee had claimed that some of the borrowed funds were used by him to introduce capital in a Firm M/s. Avi Housing Realtors but there was some dispute in this Firm. The AO has noted that the dispute with M/s. Avi Housing Realtors had been referred to an arbitrator and the arbitrator had given his award on 09.12.2013, which is prior to the Previous Year under consideration. As per the award, the assessee has received back a sum of Rs. 4.23 Crores and was also given 3 Flats costing Rs. 3.25 Crores. The AO has been considerate to hold that the borrowed funds to the tune of Rs. 3.25 Crores could be directly/indirectly be said to have converted into the 3 Flats and to that extent the borrowed funds were not available for earning interest incomes. The AO has accordingly disallowed proportionate interest of Rs. 19,62,710/-.

5. Not satisfied with the stand of the learned CIT(A) as well, the assessee is in further appeal before me.

6. I have heard the rival contentions, perused the material on record and duly considered facts of the case in the light of applicable legal position.

7. I am of the view that the rights held by the assessee in respect of three flats, which are valued by the arbitrator at Rs. 3.25 crores, cannot be considered in isolation with assessee's investment in the firm. The investment made by the assessee in the firm, to that extent, remains in existence-through in a different form because of the compulsion of a binding arbitration award rather than choice of the assessee. In this view of the matter, the disallowance of Rs. 19,62,170/- is devoid of legally sustainable and factually correct basis. I, therefore, direct the Assessing Officer to delete the impugned disallowance of Rs. 19,62,170/-

8. As I have decided the appeal on the above short ground, I see no need to deal with other issues argued by the learned representatives. Those aspects are, given the above findings, wholly academic as on now.

9. In the result, this appeal is allowed in the terms indicated above. Pronounced in the open court today on the 06th day of August 2021.

Sd/-
Pramod Kumar
(Vice President)

Mumbai, dated the 06th day of August 2021.

Copies to: (1) *The Applicant* (2) *The respondent*
 (3) *CIT* (4) *CIT(A)*
 (5) *DR* (6) *Guard File*

By order

Assistant Registrar
Income Tax Appellate Tribunal
Mumbai benches, Mumbai