

**IN THE INCOME TAX APPELLATE TRIBUNAL,  
MUMBAI BENCH "A", MUMBAI**

**BEFORE SHRI SHAMIM YAHYA, ACCOUNTANT MEMBER  
AND  
SHRI KULDIP SINGH, JUDICIAL MEMBER**

**ITA No.171/M/2021  
Assessment Year: 2015-16**

Mr. Amit Mafatlal Shah, Room No.27, 78/80, Gora Gandhi Building, 2 <sup>nd</sup> Floor, C.P. Tank Road, C.P. Tank, Mumbai – 400 004 <b>PAN: AABPS5009A</b>	Vs.	Pr.CIT-19, Room No.228, 2 <sup>nd</sup> Floor, Matru Mandir, Tardeo Road, Grant Road, Mumbai – 400 007
(Appellant)		(Respondent)

**Present for:**

Assessee by : Shri Vimal Punmiya, A.R.  
Revenue by : Ms. Shailja Rai, D.R.

Date of Hearing : 07.12.2021  
Date of Pronouncement : 21.01.2022

**ORDER**

**Per Kuldip Singh, Judicial Member:**

Appellant Mr. Amit Mafatlal Shah (hereinafter referred to as the 'assessee') by filing present appeal sought to set aside the impugned order dated 17.02.2021 passed by the Pr. Commissioner of Income Tax (the PCIT) invoking revisionary jurisdiction contained under section 263 of the Income Tax Act (hereinafter referred to as the 'Act') on the grounds inter alia that:

*“1. The Ld. PCIT erred in passing the order under section 263 of the IT Act, 1961 in spite of the fact that the assessment order was neither erroneous nor prejudicial to the interest of the revenue.*

*The Ld. PCIT erred in ignoring all the relevant facts and legal precedents cited by the appellant in support of its claim that in the facts and circumstances prevailing in the case of the appellant, no action under section 263, was called for because the two views are possible and the Ld. AO had adopted the view in favour of assessee. On the facts and circumstance of the case and law, the Ld. PCIT erred in passing order u/s 263 and thereby disallowed the deduction claimed under section 57 of Rs.32,82,266/- in respect of interest expenditure on borrowed funds.*

*2. The Assessee craves leave to add further grounds or to amend or alter the existing grounds of appeal on or before the date of hearing.”*

2. The assessee being an individual tax payee; deriving income from business, capital gain and income from other sources and house property, filed return of income declaring total income of Rs.64,34,450/-. The Assessing Officer (hereinafter referred to as AO) framed assessment under section 143(3) of the Act at the total income of Rs.4,14,84,590/- by making addition of Rs.3,43,62,880/- and Rs.6,87,257/- on account of unexplained income under section 68 of the Act and addition under section 69C of the Act respectively.

3. However, the Ld. PCIT by invoking the revisionary jurisdiction issued a notice under section 263 of the Act by flagging the issue that an interest expenditure of Rs.32,82,266/- has been incurred in respect of capital in partnership firm namely M/s. Anant Impex, income from which is exempt and sought to disallow the same under section 14A of the Act. Declining the contention raised

by the assessee the Ld. PCIT proceeded to conclude that since the assessee has incurred an interest expenditure of Rs.32,82,266/- qua assessee's capital in his partnership firm M/s. Anant Impex, income from which is exempt this interest expenditure claim has to be disallowed under section 14A of the Act and failure of the AO to do so resulted in under assessment of income of Rs.32,82,266/- and as such the assessment order is not only erroneous but prejudicial to the interest of the revenue also.

4. Feeling aggrieved from the impugned order passed by the Ld. PCIT under section 263 of the Act the assessee has come up before the Tribunal by way of filing the present appeal.

5. We have heard the Ld. Authorised Representatives of the parties to the appeal, perused the order passed by the Ld. Lower Revenue Authorities in the light of the facts and circumstances of the case and case law relied upon.

6. Undisputedly, the assessee has incurred interest expenditure of Rs.32,82,266/- in respect of capital in the partnership firm M/s. Anant Impex. It is also not in dispute that AO has raised query with regard to deduction claimed by the assessee under section 57 of the Act and by being satisfied from the explanation given by the assessee preferred not to make any addition on account of

deduction under section 57 of the Act. It is also not in dispute that in the quantum proceedings assessee's appeal for A.Y. 2015-16 also year under consideration qua order under section 263 of the Act, has already been allowed by the Tribunal vide order dated 20.04.2020 passed in ITA No.5793/Mum/2019. It is also not in dispute that assessee has filed written submissions on 10.02.2021, copy of which is available from page No.33 to 36 of the paper book, but have not been dealt with by the Ld. PCIT. It is also not in dispute that the assessee has earned taxable income from the investment made out of the borrowed fund and no exempt income has been earned during the year under assessment.

7. In the backdrop of the aforesaid facts and circumstances of this case, the sole question arises for determination in this case is as to whether it is the case of "Inadequate enquiry" on the part of AO while dealing with the issues of deduction to the tune of Rs.32,82,266/- in respect of the capital in partnership claimed by the assessee under section 57 of the Act.

8. Before proceeding further, for ready perusal we would extract the notice issued by Ld. PCIT under section 263 of the Act as under:

*"The Assessing Officer (AQ) has made assessment u/s. 143(3) of the Income Tax Act, 1967 in your case as per order dated 28.12.2017 by determining assessed income at Rs.*

*4,14,84,590/-. On perusal of scrutiny record it is seen from your Capital Account that an interest expenditure of Rs. 32,82,266/has been incurred in respect of capital in the partnership Firm M/s. Anant Impex. As per computation of income, while computing income from other Sources you have claimed deduction u/s. 57 on account of interest expenditure on borrowed funds at Rs. 34,61,758/from the interest income of Rs. 37,90,077/and the balance amount offered for income from other sources. Since you have incurred an interest expenditure of Rs. 32,82,266/in respect of your capital in your partnership firm M/s. Anant Impex, income from which is exempt this interest expenditure should have been disallowed u/s. 14A during assessment which the AO has failed to do so.*

*The AO has passed the assessment order without making necessary enquiries and verification in these aspects which should have been made to ascertain the relevant facts for the purpose of deciding the issue at hand. The assessment order therefore suffers from the infirmity and the same is erroneous in so far it is prejudicial to the interest of the revenue.”*

9. Bare perusal of the notice issued by Ld. PCIT under section 263 of the Act goes to show that Ld. PCIT has sought to disallow the interest expenditure incurred by the assessee in respect of his capital in his partnership firm M/s. Anant Impex, income from which is exempt and consequently proceeded to hold that non disallowance of interest expenditure under section 14A makes the assessment order erroneous in so far as prejudicial to the revenue's interest.

10. It is pertinent to bring on record that Ld. PCIT has issued the notice under section 263 of the Act pointing out that AO was required to disallow the interest expenditure of Rs.32,82,266/- under section 14A of the Act, whereas in the impugned order

passed under section 263 of the Act Ld. PCIT sought to disallow the deduction claimed under section 57 of the Act in respect of capital in partnership firm by the AO. For facility of reference the operative part of the impugned order passed by Ld. PCIT is as under:

*“I have gone through the assessment records and examined the submissions made by the assessee. After careful examination of the assessment records and reply of the assessee, has come to the conclusion that the assessee has failed to establish the nexus between the utilisation of interest bearing funds and has not proved that taxable income has been earned from interest bearing funds. The Assessing Officer has committed an error causing prejudice to revenue by allowing the assessee’s claim of deduction u/s 57 on account of interest expenditure on borrowed funds at Rs.32,82,266/- from the interest income of Rs.37,90,077/-. The Assessing Officer has failed to carry out necessary enquiries as warranted by the facts and circumstances of the case and apply the provisions of the law as discussed above, Thus the assessments are found to be erroneous in so far as it is prejudicial to the interest of revenue as envisaged in section 263 of the I.T. Act. **There is lack of enquiry by the Assessing Officer on the issue raised in the notice issued u/s 263 of the Act. The Assessing officer may have disallowed the deduction claimed u/s 57 Rs.32,82,266/- in respect of capital in partnership firm.**”*

11. It is settled principle of law that in order to invoke the provisions contained under section 263 of the Act the Ld. PCIT is required to pass the twin test viz.:-

- “That the assessment order passed by the AO is erroneous and
- That in so far as it is prejudicial to the interest of the Revenue.”

12. So far as question of terming the assessment order erroneous by Ld. PCIT is concerned, he has proceeded on the premise that the AO should have disallowed the deduction of Rs.32,82,266/- claimed by the assessee under section 57 of the Act in respect of the capital in partnership firm for which no notice under section 263 of the Act has been given. The Ld. A.R. for the assessee, by relying upon notice issued by the AO during the assessment proceedings under section 142(1)/129 of the Act which is available at page No.17 of the written submissions of paper book and written reply dated 10.02.2021 filed by the assessee before the AO duly explaining the reason for claiming deduction under section 57 of the Act is available at page No.32 to 36 of paper book -I, contended that complete enquiry has been conducted by the AO and after being satisfied he has allowed the deduction claimed by the assessee under section 57 of the Act.

13. We have perused the copy of notice issued by the AO under section 142(1) & 129 of the Act seeking reasons for large deduction under section 57 of the Act and reply filed by the assessee thereto furnishing complete reasons wherein it is duly explained that in order to avail the deduction under section 57 of the Act three conditions must be complied inter-alia that the capital must have

been borrowed; interest must have been paid; and that funds must have been borrowed for the purpose of business.

14. It is undisputed fact that the assessee has borrowed the funds on which interest expenditure of Rs.32,82,266/- has been incurred in respect of capital in partnership firm M/s. Anant Impex. It is also not in dispute that during the year under assessment the assessee has earned interest income from three parties on borrowed funds from M/s. Anant Impex to the tune of Rs.34,61,758/-. When the assessee has borrowed the fund for capital in partnership firm concerned it has to be treated having been borrowed for the purpose of business.

15. When this fact is examined in the light of the fact that assessee has earned taxable income from the investment made from the borrowed fund, section 14A is not attracted as no exempt income has been earned. When no exempt income has been earned no disallowance under section 14A is to be made as has been held by Hon'ble Delhi High Court in the case of Cheminvest Ltd. vs. CIT reported in (2015) 378 ITR 33.

16. Moreover, when the assessee has borrowed funds from the partnership firm and paid interest to the partnership firm in his individual capacity again section 14A is not attracted. Had the

assessee borrowed funds on interest and invested in item whose income is exempt then interest would not have been allowed as expenses, rather it is a case of earning taxable income from the investment made from the borrowed funds. So we are of the considered view that on duly explaining by the assessee the AO has taken plausible view and rightly allowed the deduction claimed by the assessee under section 57 of the Act, hence assessment order cannot be termed as erroneous and in so far as prejudicial to the interest of the Revenue.

17. Moreover, when we examine the notice issued by the Ld. PCIT under section 263 of the Act and impugned order passed thereafter the Ld. PCIT was himself not clear enough as to whether he sought to disallow the interest expenditure under section 14A of the Act and has mentioned in the notice or sought to disallow the deduction claimed by the assessee under section 57 of the Act as has been held in the impugned order. We are of the considered view that order under section 263 of the Act has to be passed in consonance with the notice issued under section 263 of the Act.

18. Moreover, it is undisputed fact on record that in the preceding two years the AO had also allowed deduction on account of interest expenditure under section 57 of the Act and Revenue has accepted the same. So when the borrowed funds have not been

invested in the item whose income is exempt the interest has to be allowed as claimed by the assessee.

19. So we are of the considered view that when the AO was duly satisfied with the reasoning brought on record by the assessee in reply to the notice issued under section 142(1) of the Act and allowed the deduction claimed under section 57 of the Act by duly applying his mind, it is neither a case of no enquiry nor a case of non application of mind by the AO, thus proceedings under section 263 of the Act cannot be initiated. Resultantly, the impugned order passed under section 263 of the Act is not sustainable in the eyes of law hence order to be quashed.

20. The appeal filed by the assessee is hereby allowed.

**Order pronounced in the open court on 21.01.2022.**

**Sd/-  
(SHAMIM YAHYA)  
ACCOUNTANT MEMBER**

**Sd/-  
(KULDIP SINGH)  
JUDICIAL MEMBER**

Mumbai, Dated: 21.01.2022.

\* Kishore, Sr. P.S.

Copy to: The Appellant  
The Respondent  
The CIT, Concerned, Mumbai

The CIT (A) Concerned, Mumbai  
The DR Concerned Bench

//True Copy//

By Order

Dy/Asstt. Registrar, ITAT, Mumbai.