

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

BEFORE SHRI ABY T VARKEY, HON'BLE JUDICIAL MEMBER

&

SHRI S. RIFAUR RAHMAN, HON'BLE ACCOUNTANT MEMBER

ITA NO. 2755/MUM/2023 (A.Y: 2016-17)

Shri Shreepal Babulal Bafna Flat No. 502, 5 th Floor Kumar Sophronia CHS Shri Adeshwar Bhagwan Marg Byculla (E), Mumbai - 400027 PAN: AAEPB7981K (Appellant)	v.	Income Tax Officer – Ward – 23(3)(6) Room No. 606, 6 th Floor Earnest House Nariman Point, Mumbai - 400021 (Respondent)
---	----	---

Assessee Represented by	:	Shri Nitesh Jain
Department Represented by	:	Shri S.N. Kabra
Date of Conclusion of Hearing	:	29.11.2023
Date of Pronouncement	:	13.12.2023

ORDER

PER S. RIFAUR RAHMAN (AM)

1. This appeal is filed by the assessee against order of Learned Commissioner of Income Tax (Appeals), National Faceless Appeal Centre, Delhi [hereinafter in short "Ld.CIT(A)"] dated 22.05.2023 for the A.Y.2016-17.

2. Brief facts of the case are, Assessee is an Individual, deriving Income from House Property, Income from Business and income from Other Sources. Assessee filed his return of Income on 20.09.2016, declaring total Income of ₹.NIL. The assessment was originally completed u/s. 143(1) accepting the returned income. Subsequently, the case was selected for scrutiny proceedings u/s. 143(2) of the Income-tax Act, 1961 (in short "Act"). During the course of assessment proceedings, authorised representative of the Assessee filed the details from time to time on e-portal and manually.

3. During the year under consideration, Assessee has claimed expense of ₹.47,69,513/- on account of interest paid/payable on unsecured loans taken. Assessing Officer issued notice dated 13.11.2018 asking the assessee as to why interest on unsecured loan amounting to ₹.40,89,280/- should not be disallowed u/s. 36(1)(iii) of the Act, on the plea that the interest expense claimed has not yet been paid or borrowed funds not fully utilized for business purpose.

4. In response, authorised representative of the Assessee filed the submission vide letter dated 15.11.2018. After considering the submissions of the assessee, Assessing Officer rejected the said

submission and disallowed the interest expenses amounting to ₹.40,89,280/- u/s. 36(1)(iii) of the Act and passed an assessment order u/s. 143(3) of the Act on 20.11.2018 by assessing the Total Income of ₹.40,95,120/-.

5. Aggrieved assessee preferred appeal before the Ld. CIT(A) and filed detailed submissions before Ld. CIT(A). After considering the submissions of the assessee Ld. CIT(A) sustained the addition made by the Assessing Officer.

6. Aggrieved assessee filed appeal before us raising following grounds in its appeal: -

"1) On the facts and under the circumstances of the case and in law, the learned Assessing Officer has erred in disallowing interest expenses amounting to Rs. 40,89,280/- u/s. 36(1)(iii) of the Act and the reasons assigned for doing so are wrong and contrary to the facts and the provision of the law.

2) The appellant craves leaves to add, alter, amend, modify or withdraw all or any of the ground of appeal on or before the date of hearing."

7. At the time of hearing, Ld.AR of the assessee brought to our notice relevant facts of the case and submitted as under: -

"i.) During the course of assessment proceedings, the learned AO had emphasized on the fulfillment of three fundamental conditions

of Section 36(1)(iii) of the Act for allowing the Interest expenditure which are as under:

- a. The assessee must have borrowed money
- b. The money so borrowed must have been used for the purpose of business
- c. Interest is paid or payable on such borrowing.

ii.) After considering all the submissions of the Appellant, the learned AO opined that:

- a. The first condition i.e. the assessee must have borrowed money was satisfied.
- b. The second condition i.e. money so borrowed must have been used for the purpose of business was satisfied to the extent as under:

Particulars		Amount in Rs.
Total interest-bearing borrowings	A	4,74,38,989
Total interest-bearing investments out of interest-bearing borrowings	B	3,06,81,539
Total inter-bearing borrowings used for personal obligations	C (A-B)	1,24,62,188
Proportionate Interest to be disallowed (@12%)		14,95,462

- c. The third condition i.e. Interest is paid or payable on such borrowing was not satisfied.

iii.) During the course of appellate proceedings, the Appellant had again submitted all the details and documents submitted before the Id. AO. After considering our submission, the Hon'ble CIT(A) opined as under.

- a. the first condition i.e., the assessee must have borrowed money was satisfied.
- b. The second condition i.e. money so borrowed must have been used for the purpose of business was not fully satisfied.
- c. the third condition i.e. Interest is paid or payable on such borrowing was satisfied.

iv.) As per the above findings, the only condition which is not fully satisfied for allowance of deduction u/s. 36(l)(iii) of the Act is the second condition i.e. The money so borrowed must have been used for the purpose of the business.

However, the average interest rate of Interest should be worked out as under:

Particulars		Amount in Rs.
Total interest-bearing borrowings	A	4,74,38,989
Total Interest Expenditure claimed	B	47,69,513
Avg. Rate of Interest	C(A/B)	10.05%

Hence, the proportionate disallowance of Interest should be worked out as under:

Particulars		Amount in Rs.
Total interest-bearing borrowings	A	4,74,38,989
Total interest-bearing investments out of interest-bearing borrowings	B	3,06,81,539
Total inter-bearing borrowings used for personal obligations	C (A-B)	1,24,62,188
Proportionate Interest to be disallowed (@ 10.05%)		12,52,450

v.) Therefore, we pray to your Honour to restrict the disallowance made by the Ld. AO to Rs. 12,52,450/- to meet the ends of justice."

8. On the other hand, Ld. DR relied on the findings of Assessing Officer and brought to our notice Page No. 3 of the assessment order and Page No. 10 of the appellate order. He submitted that the findings of the lower authorities may be sustained.

9. Considered the rival submissions and material placed on record, we observe from the record that assessee has borrowed funds from various parties and the statement submitted by the assessee [which is placed on

record] shows that the assessee has borrowed funds from 27 parties and all these parties are existing parties through whom assessee has borrowed most of the loans in earlier assessment years and only four parties i.e., Jheel R Jain, Kalpataru Diamonds, Madanlal A shah HUF and Mangiilal Okhchandji Jain HUF] from whom assessee has taken fresh loan during the year. Also we observe that to some of the parties assessee has repaid the loans. During the year assessee has credited the interest of ₹.47,69,513/- to the above said parties and it is also relevant to note that to some of the parties, assessee has not provided any interest payment. At the end of the financial year assessee carried forward unsecured loans of ₹.4,74,38,989/- which includes the interest provided to the parties and whatever interest provided by the assessee the assessee has paid the interest in the subsequent financial years. However, we observe that the tax authorities have taken a view that assessee has not fulfilled the conditions specified under section 36(1) of the Act as per which assessee must have borrowed the money, money so borrowed must have been used for the purpose business and the interest is paid was payable on such borrowings. In the given case both Assessing Officer and Ld. CIT(A) has accepted that assessee has borrowed the money and money was used in the business. However, due to the fact that assessee has only provided for the interest during the year and not paid the interest before filing the

return of income they came to the conclusion that assessee is not eligible to claim the above said interest expenditure. However, on the contrary we observe that assessee has borrowed the funds from various parties and majority of the funds were used by the assessee by lending the money to the partnership firm in which assessee is one of the partner. From the computation of income and income and expenditure account submitted before us clearly shows that assessee has claimed the interest expenditure of ₹.47,69,513/- and at the same time assessee has received interest from the partnership firm to the extent of ₹.31,95,914/-. Therefore, as per the provisions of section 36(1) of the Act assessee has borrowed funds and utilized the same in its business to the extent of funds utilized by the assessee in the partnership firm should be considered as applied for the purpose of business. Therefore, in our considered view to the extent of funds applied by the assessee for the purpose of business should be allowed as business expenditure. Therefore, as per record assessee has claimed interest expenditure of ₹.47,69,513/- and to the extent of funds applied for the purpose of business i.e., investment in Firm through which assessee has received interest ₹.31,95,914/- from the partnership firm and the balance may be disallowed which was utilized for other than business purposes. Accordingly, the grounds raised by the assessee is

accordingly partly allowed and we direct the Assessing Officer to disallow only to the extent of ₹.15,73,599/-.

10. In the result, appeal filed by the assessee is partly allowed.

Order pronounced in the open court on 13th December, 2023.

Sd/-
(ABY T VARKEY)
JUDICIAL MEMBER

Mumbai / Dated 13.12.2023
Giridhar, Sr.PS

Sd/-
(S. RIFAUH RAHMAN)
ACCOUNTANT MEMBER

Copy of the Order forwarded to:

1. The Appellant
2. The Respondent.
3. CIT
4. DR, ITAT, Mumbai
5. Guard file.

//True Copy//

BY ORDER

(Asstt. Registrar)
ITAT, Mum