

आयकर अपीलीय अधिकरण, 'ए' न्यायपीठ, चेन्नई  
IN THE INCOME-TAX APPELLATE TRIBUNAL 'A' BENCH, CHENNAI  
श्री वी दुर्गा राव न्यायिक सदस्य एवं श्री जी. मंजुनाथा, लेखा सदस्य के समक्ष  
Before Shri V. Durga Rao, Judicial Member &  
Shri Manjunatha, G., Accountant Member

आयकर अपील सं./I.T.A. Nos.3273 & 3274/Chny/2018  
निर्धारण वर्ष/Assessment Years: 2014-15 & 2015-16

M/s. Devraj Computers Pvt. Ltd.,  
No. 42, Gee Gee Complex, 3<sup>rd</sup> Floor,  
Mount Road, Chennai 600 002.  
**[PAN:AABCD1593P]**

Vs. The Assistant Commissioner of  
Income Tax, Corporate Range – 1,  
Chennai.

(अपीलार्थी/Appellant)

(प्रत्यर्थी/Respondent)

अपीलार्थी की ओर से / Appellant by : Shri D. Anand, Advocate  
प्रत्यर्थी की ओर से/Respondent by : Shri AR V Sreenivasan, Addl. CIT  
सुनवाई की तारीख/ Date of hearing : 05.02.2024  
घोषणा की तारीख /Date of Pronouncement : 21.03.2024

**आदेश /O R D E R**

**PER V. DURGA RAO, JUDICIAL MEMBER:**

Both the appeals filed by the assessee are directed against common order of the Id. Commissioner of Income Tax (Appeals) 1, Chennai, dated 27.09.2018 relevant to the assessment years 2014-15 & 2015-16. In the grounds of appeal, the assessee has raised following common grounds for both the assessment years:

**GROUND OF APPEAL**

- The order passed by the learned Assistant Commissioner of Income Tax, Corporate Range-1, Chennai 34 is against the facts of the case and principles of natural justice.*
- The learned Commissioner of Income Tax (Appeals) -1 made arbitrary additions without the right application of law.*

3. *The learned Commissioner of Income Tax (Appeals) - I arbitrarily made additions on account of interest lost due to interest free advances made by the appellant, disregarding the fact that the same was advanced during the normal course of business.*
4. *The learned Commissioner of Income Tax (Appeals) - I failed to appreciate the fact that the appellant had sufficient interest free funds in the form of capital reserves and other funds without interest to cover funds given interest free or utilized other than for business purpose.*
5. *The learned Commissioner of Income Tax (Appeals) - I failed to appreciate the cash flow comparisons provided for various year wherein it was duly substantiated that the company's free capital was any time more than the interest free advances.*

*For these and other reasons that may be adduced during the course of hearing it is hereby sincerely prayed that the additions may kindly be deleted and thus render justice.*

2. Brief facts of the case are that the assessee is engaged in the business of trading in computer accessories and filed its return of income for the assessment year 2014-15 on 30.09.2014 admitting a total income of ₹.63,83,550/-. After considering the submissions of the assessee against statutory notices, the Assessing Officer has completed the assessment under section 143(3) of the Income Tax Act, 1961 ["Act" in short] after disallowing a sum of ₹.28,46,684/- on account of interest costs incurred by the assessee attributable towards interest-free loans and advances made to related parties as well as disallowance of puja expenses of ₹.2,46,850/- and disallowance under section 40A(3) of the Act at ₹.54,426/-. Similarly, assessment for the assessment year 2015-16 has been completed after disallowing a sum of ₹.14,39,276/- on account

of interest cost attributable to interest-free loans and advances and a sum of ₹.1,45,215/- towards puja expenses.

3. With regard to the disallowance of interest claimed by the assessee to the extent of ₹.28,46,684/-, the assessee has utilized the interest-bearing funds towards making interest free loans and advances to various related parties. The Assessing Officer has observed that during the previous year the assessee had outstanding unsecured loan to the extent of ₹.4,30,56,985/- on which the sum of ₹.29,69,040/- was incurred as interest cost. The assessee has also availed secured loan from bank to the extent of ₹.3,93,69,820/-. The assessee has claimed a total sum of ₹.69,44,555/- as interest cost in its P&L account against all these borrowings. The Assessing Officer has observed that against these borrowings which are interest-bearing, the assessee has advanced a sum of ₹.4,14,60,482/- to various related parties. Out of the total amount advanced, only a sum of ₹.76,51,884/- was an interest-bearing advance. The balance outstanding amount advanced by the assessee is on interest-free basis. Therefore, the Assessing Officer has concluded that the interest-bearing funds of the assessee have been partly utilized towards advancing loan to various related parties. Accordingly, the Assessing Officer computed the interest attributable towards the

amounts advanced on interest-free basis to related parties at ₹.28,46,684/- for assessment year 2014-15. Similarly, in the assessment year 2015-16, the Assessing Officer made disallowance of interest made to the extent of ₹.14,39,276/- on account of utilization of interest-bearing funds towards advancing interest-free loans and advances to related parties.

4. The assessee carried the matter in appeal before the Id. CIT(A) for both the assessment years. The queries raised by the Id. CIT(A), submissions of the assessee and the observations of the Id. CIT(A) are as under:

*7. The primary contention of the appellant was that it was for the Assessing Officer to establish the diversion of interest-bearing funds towards loans and advances on interest-free basis. It was also the appellant's grievance that sufficient opportunity was not given to establish the fact that substantial loans and advances were actually in the nature of trade advance. The appellant also submitted that they were not given proper opportunity to explain how the interest-free funds were sufficient to make the loans and advances to related parties on interest-free basis. Accordingly, the appellant was given a number of opportunities and in particular hearings were granted to the appellant on 25.7.2018, 7.8.2018 and 24.9.2018. The appellant was specifically asked to show:*

- a. how the interest-free loans and advances made to related parties were financed by the appellant out of interest-free funds on a year-to-year basis, particularly when the appellant contended that most of these advances were made in earlier years.*
- b. The appellant was requested to produce the balance sheet of the relevant assessment years to show that in those years sufficient interest-free funds were available with the appellant to make the interest-free loans and advances to related parties.*
- c. To submit the breakup of the total interest paid towards various loans outstanding during the year.*

- d. *To furnish complete details of the interest-free loans and advances made to related parties and segregating the same into interest-bearing and interest-free loans.*
- e. *To give evidence for loans and advances claimed to be advanced in the course of business.*
8. *In response to these queries raised the appellant has submitted only partial information. The appellant has made their submissions in the letters dated 16.8.2018 and 26.9.2018.*
- a. *The appellant has firstly submitted that the total share capital of the appellant at Rs.12,8,23,125/- and the profits earned from year to year from 2009 to 2014 should be assumed to have been utilized towards making the interest-free loans and advances.*
- b. *The appellant has secondly submitted that the loans and advances account (loans to related parties on interest free basis) showed an outstanding of Rs.1,95,70,270/- as on 31.3.2009 which was prior to the secured loan raised by the appellant from Yes Bank on which part of the interest claimed during the year has been paid. Thus, it was contended that the Yes Bank loan could not have been utilized for advancing loan to related parties.*
- c. *The appellant submitted that the source and' application of funds should be seen on a larger perspective as the appellant maintained a common pool of funds and while temporary arrangement of funds could be made from interest-bearing sources, over a period of time the interest-free funds were sufficient to finance the interest-free loans to related parties. It is submitted by the appellant that the interest-free funds of the appellant is more than 50% of the interest-free loans and advances made by the appellant.*
- d. *it is also submitted that interest-free advances were tactical business investments for the benefit of the company.*
- e. *The appellant placed on record the balance sheet for the year ended 31.3.2009 and a summary of the funds flow statement prepared from year to year from 2009 to 2015.*
9. *The appellant's contentions are considered. All the information relating to the sources of funds are available in the hands of the appellant from year to year and their application towards interest-free advances are also available only with the appellant. Therefore, it is for the appellant to establish that interest free funds were available in sufficient quantity to make the interest-free loans and advances to related parties. A prima facie case has been made out by the Assessing Officer to the extent that during the previous year the appellant has substantial borrowed funds on which interest cost has been incurred and an equal amount of interest-free loans and advances made to related parties. Therefore, the onus is on the appellant to establish that they had sufficient interest-free funds available at the relevant point of time to make the advance to related parties on interest-free basis.*

10. According to the appellant the interest-free loans and advances were made even prior to 31.3.2009 whereas the secured loan from Yes bank on with substantial interest has been paid during the year has been obtained thereafter. In support of this contention the appellant has placed on record the balance sheet as on 31.3.2009. As per schedule 6 of the said Balance Sheet the details of loans and advances made have been provided. A reference to the said schedule indicates that most of these advances are in the nature of deposits given in the course of business such as telephone deposit, electricity deposit, earnest money deposit, advance taxes and duties etc. None of the related parties in respect of whom there are outstanding balances at the end of the relevant assessment year, appear as outstanding appear in the Schedule as on 31.3.2009. Therefore, the appellant's contention that the loans and advances to the related parties were made prior to 2009 i.e. even before the loan was availed from Yes bank is factually incorrect.

11. As regards the appellant's contention that some of the parties to whom loan and advances were made on interest-free basis were in the nature of a trade advance, no evidence in this regard was submitted by the appellant during the appeal proceedings or before the Assessing Officer. Therefore, for want of evidence this contention of the appellant is rejected.

12. As regards the appellant's contention that they had substantial funds in the form of share capital and profits earned from year to year and the same should be held as applied towards making the interest-free loans in advance to related parties, while the same can be accepted as a general proposition, it is for the appellant to still establish that these interest-free funds were in fact available with the appellant at the time when the interest free advances were made to related parties. It is also to be observed that the appellant itself has admitted that they maintained a common pool of funds so that the interest-bearing funds as well as the interest refunds are all accumulated together and from the common pool the funds are drawn both towards business purposes as well as to make advances to related parties on interest-free basis. (appellant's letter dated 16.8.2018 page 3). Under such a situation it is for the appellant to establish that in the year when the interest-free advances were made to related parties, the appellant had sufficient interest-free funds available with them.

13. As regards the actual funds flow position the appellant has given a tabular form of the cash flow statement prepared along with the balance sheet on a year-to-year basis from 2009 to 2015. The fact that the statement is provided from the year ending March 2009 implies that the interest free loans and advances were made only after March 2009. This is also corroborated by Schedule 6 of Balance sheet for 2008-09 referred earlier in para 10. It is observed from the same that during the year ended 31.3.2010 short-term loans and advances made by the appellant has increased to the extent of Rs.46,57,580/-. In the same year there is an increase in long-term borrowings to the extent of Rs.56,99,152/-. Similarly, in the year ended 31.3.2014 while there is an increase in the short-term loans and advances made by the appellant to the extent of Rs.24,54,352/-, there is an increase in the long-term borrowings during the same to the extent of Rs.3,93,69,821/-. Similarly it is found that for the year ended March 2013 while the short-term loans and advances have increased to the extent of Rs.87,70,330/-, the short-term borrowings during the same period have also increased to the extent of Rs.1,50,87,972/-. Similarly, while the loans and advances given to related parties as increased to the extent of Rs.5,16,839/- in the year ended 31.3.2015, in the same period the short-term

*borrowings received by the appellant has also increased to the extent of Rs.1,30,33,465/-. This shows that in all the years when the appellant advanced new loans or advance to related parties to the extent of Rs.1,63,99,101/-, there is also an increase in the short-term borrowings and long-term borrowings made by the appellant, The appellant has failed to show how the interest-free funds were available at the relevant point of time to fund these increases in the short-term loans and advances. Under the circumstances, it is held that the appellant has failed to establish any nexus between the interest-free funds available with the appellant and the interest free loans and advances made to related parties. On the other hand the analysis of the cash flow statement shows that there is nexus between borrowed funds and loans and advances made to related parties to the extent of Rs.1,63,99,101/- [Rs.46,57,580/- + Rs.24,54,352/- + Rs.87,70,330/- + Rs.5,16,939/-]. Therefore, the disallowance is sustained to the extent of proportionate interest attributable to loan of Rs.1.63 crores out of total loan of Rs.4.14 crores to related parties. This ground of appeal is partly allowed.*

5. On being aggrieved, the assessee is in appeal before the Tribunal.

The Id. Counsel for the assessee has submitted that based on the cash flow statement, the Id. CIT(A) has erroneously held that there is nexus between borrowed funds and loans and advances made to related parties to the extent of ₹.1,63,99,101/-. It was further submission that the sum of ₹.76,51,884/- was only an interest-bearing advance, which has to be reduced from the amount of ₹.1,63,99,101/-, sustained by the Id. CIT(A).

6. On the other hand, the Id. DR strongly supported the orders of authorities below.

7. We have heard both the sides, perused the materials available on record and gone through the orders of authorities below. The Assessing Officer has computed the interest attributable towards the amounts advanced on interest-free basis to related parties at ₹.28,46,684/-. In the

assessment order for the assessment year 2014-15, the Assessing Officer has noted that out of overall interest bearing borrowals, the assessee has advanced a sum of ₹.4,14,60,482/- to various related parties. The Assessing Officer further noted that out of total loans and advance of ₹.4,14,60,482/- given to various related parties, the assessee has charged interest on a sum of ₹.76,51,884/- and the balance has been given as interest free loans to parties and thus computed proportionate interest and disallowed under section 36(1)(iii) of the Act. The Id. CIT(A), based on the cash flow statement from 2009-2015, has computed utilization of interest bearing funds for the purpose of giving interest free loans and advances to related parties for each year and total of such interest bearing funds advanced to related parties for 4 years worked out to ₹.1,63,99,101/- and the said findings have been recorded in para 13 of Id. CIT(A)'s order. In fact, the assessee is not disputing the interest bearing funds worked out by the Id. CIT(A). The only grievance of the assessee is that the sum of ₹.1,63,99,101/- is included the sum of ₹.76,51,884/- on which the assessee has charged interest and the Assessing Officer has allowed but credit should have been given before arriving at the net interest bearing funds used for giving interest free loans. We find that the Assessing Officer has accepted the fact that the assessee has charged interest on ₹.76,51,884/-, but, the Id. CIT(A), while

computing the net amount of interest bearing funds based on the cash flow statement, has failed to give credit to the amount of loan on which interest has already been charged by the assessee. Therefore, we of the considered opinion that since there is no dispute on the fact that a sum of ₹.76,51,884/- has already been considered for charging interest, the said amount should be deducted from net interest bearing fund of ₹.1,63,99,101/- worked out by the Id. CIT(A) for the purpose of charging interest under section 36(1)(iii) of the Act. Thus, we modify the findings of the Id. CIT(A) on this issue and direct the Assessing Officer to reduce the sum of ₹.76,51,884/- from the total amount of interest bearing funds computed by the Id. CIT(A) at ₹.1,63,99,101/- and for balance amount, compute proportionate interest and disallow under section 36(1)(iii) of the Act.

8. For assessment year 2015-16, the Assessing Officer has calculated the proportion of the interest expenditure out of the borrowed funds attributable to interest free loans and advances at ₹.14,39,276/-. The Id. CIT(A) has worked out interest bearing funds of ₹.1,63,99,101/- and directed the Assessing Officer to compute proportionate interest and disallow for the assessment year 2015-16 also. Since we have already considered this issue for the assessment year 2014-15 and held that out

of ₹.1,63,99,101/-, the sum of ₹.76,51,884/- has to be reduced because the assessee has already charged interest on loans given to related parties the sum of ₹.76,51,884/-. Therefore, we modify the findings of the Id. CIT(A) and direct the Assessing Officer to compute proportionate interest disallowable under section 36(1)(iii) of the Act after reducing the sum of ₹.76,51,884/- from the total interest bearing funds computed by the Assessing Officer of ₹.69,00,000/- of net interest bearing funds and disallow under section 36(1)(iii) of the Act.

9. In the result, both the appeals filed by the assessee are partly allowed.

Order pronounced on 21<sup>st</sup> March, 2024 at Chennai.

Sd/-  
(MANJUNATHA, G.)  
ACCOUNTANT MEMBER

Sd/-  
(V. DURGA RAO)  
JUDICIAL MEMBER

Chennai, Dated, 21.03.2024

Vm/-  
आदेश की प्रतिलिपि अग्रेषित/Copy to:

1. अपीलार्थी/Appellant,
2. प्रत्यर्थी/ Respondent,
3. आयकर आयुक्त/CIT,
4. विभागीय प्रतिनिधि/DR &
5. गार्ड फाईल/GF.