

आयकर अपीलीय अधिकरण, हैदराबाद पीठ में
**IN THE INCOME TAX APPELLATE TRIBUNAL
HYDERABAD BENCHES "A", HYDERABAD**

BEFORE

**SHRI LALIET KUMAR, HON'BLE JUDICIAL MEMBER
AND
SHRI MANJUNATHA G, HON'BLE ACCOUNTANT MEMBER**

ITA No.691/Hyd/2020		
Assessment Year: 2017-18		
M/s. Kausalya Management Services and Structures Private Limited, Karimnagar. PAN : AAECK9304L (Appellant / Assessee)	Vs.	The Deputy Commissioner of Income Tax, Central Circle – 2(3), Hyderabad. (Respondent)
Assessee by:	Shri S. Ramarao, Advocate	
Revenue by:	Ms. Reema Yadav, Sr.AR.	
Date of hearing:	12.08.2024	
Date of pronouncement:	04.09.2024	

ORDER

PER BENCH :

This appeal filed by the assessee is directed against the order of learned Commissioner of Income Tax (Appeals) – 12, Hyderabad dated 18.09.2020 for the assessment year 2017-18.

2. The grounds raised by the assessee read as under :

“1. The order of the ld.CIT(A) is erroneous both on facts and in law.

2. The ld.CIT(A) erred in confirming the addition of Rs.83,15,248/- out of the total disallowance made of Rs.4,45,90,074/- without allowing the entire amount as an allowable deduction.

3. The ld.CIT(A) erred in holding that there was diversion of funds borrowed for the purpose of business and that the interest debited to the profit and loss account is not an allowable deduction.

4. The ld.CIT(A) erred in considering the trade payables as the borrowed funds for the purpose of working out the disallowance of interest.

5. The ld.CIT(A) ought to have considered the fact that no income arose on account of the investment made and, therefore, no disallowance should have been made by the Assessing Officer.”

3. The brief facts of the case are that the appellant is a private limited company engaged in the business of construction and sale of residential and commercial flats. The assessee has filed its return of income for the assessment year 2017-18 on 18.10.2017 declaring Nil income. A search and seizure operation under Section 132 of the Act was conducted on 07-04-2017 on the assessee, as part of the search conducted on M/s.Kapil Consultancy Services Pvt. Ltd. and others. Consequent to the search, the assessment was completed under Section 143(3) of the Income Tax Act, 1961 on 30-12-2019 and determined the total income at Rs.4,53,60,573/- by making additions towards disallowance of finance charges and disallowance under Section 14A of the Act.

4. On appeal, the ld. CIT(A) for the reasons stated in their order dated 18.09.2020 had confirmed the addition made towards disallowance of finance charges to an extent of Rs.83,15,248/-, however, deleted the addition made under Section 14A of the Act.

5. The assessee preferred a further appeal before the ITAT, and the ITAT, vide its common order in ITA No.691/Hyd/2020 dated 21-03-2022, set aside the issue to the file of AO for verification. The assessee filed an appeal before the Hon'ble High Court of Telangana against the common order passed by the Tribunal and contested that the Tribunal can decide only those issues which are subject to appeal before the Tribunal, and the issues already decided by the ld. CIT(A) and not challenged by the Department cannot be decided, nor can the appeal be set aside in total. The Hon'ble High Court of Telangana vide its order dated 02-02-2023, set aside the common order of the Tribunal passed on 21-03-2022, and directed the Tribunal to hear the appeals before it on the limited grounds urged by the appellant, namely, disallowance of finance charges under Section 36(1)(iii) of the Act to the extent disallowed by the first appellate authority as well as the validity of the reassessment proceedings.

6. The solitary issue that came up for our consideration in Ground Nos.2 to 5 of the assessee's appeal is the disallowance of finance charges of Rs.83,15,248/- confirmed by the Id.CIT(A) under Section 36(1)(iii) of the Income Tax Act, 1961. During the course of the assessment proceedings, the AO noticed that the real estate companies of Kapil Group have been accepting advance for sales of residential / commercial office space by entering into an MOU with potential customers. As per the MOU, the potential customer has to pay 80% of the sale consideration and choose an advance PUT option for redeeming the advance given. Depending upon the period of advance PUT option, interest will be paid ranging from 10% to 14%. The potential customer can get the office space or flat registered by paying the balance 20% of the consideration before the advance PUT option period ended. If the potential customer withdraws the advance amount earlier to advance PUT option, he will be given much lesser interest than the promised interest. The AO observed that as per Schedule 17 annexed to the Profit and Loss Account filed by the assessee, an amount of Rs.5,52,73,977/- has been claimed as interest charges under the head Revenue Expenses and added to work-in-progress. The AO called upon the assessee to file necessary evidence and also justification for the interest debited under the head Revenue Expenses added to work-in-progress. In response, the assessee submitted that it has paid interest amounting to Rs.5,52,73,977/- to customers on advance paid by them in light of MOUs and as the same was incidental to the business, it has debited to the Profit and Loss Account. However, the said amount was taken to the balance sheet under the head work-in-progress for claiming the same proportionately against the revenue from sale of flats in the future. The assessee further

submitted that since the customer has paid an advance amount of about 80% of the sale value, as per the agreement with the customers, the appellant has paid interest ranging from 10% to 14% for a period of 1 year to 4 years. Therefore, the assessee submitted that interest paid on customer advances was wholly and exclusively for the purpose of the business of the assessee and thus, allowable as a deduction.

7. The AO, however, was not convinced with the explanation furnished by the assessee. According to the AO, although the assessee has furnished general reply regarding the purpose of the funds received as an advance for the purchase of office space, but failed to explain the utility of the advances for the purpose of the business of the assessee. The AO further observed that the appellant has diverted advances received from customers to various other group companies. Therefore, the AO opined that the interest paid can not be justified just because TDS has been deducted on the said interest. Accordingly, the AO disallowed the interest debited under finance charges and carried forward to work-in-progress amounting to Rs.4,45,90,074/- under Section 36(1)(iii) of the Income Tax Act, 1961.

8. The assessee carried the matter in appeal before the Id. CIT(A). Before the Id. CIT(A), the assessee submitted that the interest paid on customers' advance is wholly and exclusively incurred for the purpose of business and further, the assessee has paid interest on customers' advance, as per the terms of MOU with customers.

The Id. CIT(A), after considering the relevant submissions of the assessee and also taken note of the fact that the assessee has made investments in various group companies, amounting to Rs. 7,70,49,950/- whereas own funds being shareholder funds and long-term borrowings is not sufficient to cover investments and thus, opined that the appellant diverted funds to the tune of Rs. 6,92,93,735/-, therefore, worked out interest expenses @ 12% of Rs.6,92,93,735/- on funds diverted to other group companies and partly confirmed the addition made by the AO towards disallowance of finance charges.

9. The learned counsel for the assessee, Shri S. Rama Rao, submitted that the Id. CIT(A) is erred in sustaining the addition made by the AO towards disallowance of finance charges on altogether a different ground, even though, the AO disallowed interest on the ground that the appellant has not established utilization of advances from customers for the purpose of business of the assessee. The learned counsel for the assessee further submitted that the assessee is into the business of real estate development, collects advances from customers for sale of residential flats and commercial space. The customers pay 80% of consideration in advance in terms of MOU. The MOU provides for payment of interest @ of 10% to 14% in case of delay in delivery of flats. As per the agreement between customers, the appellant has paid interest on customers' advance and the same has been debited under the head finance charges. The Id.CIT(A) without appreciating the relevant facts, confirmed the addition to an extent of Rs.83,15,248/- out of

the total disallowance of Rs.4,45,90,074/- and the order should be set aside.

10. The ld.DR Ms. Reema Yadav, on the other hand, supporting the order of ld. CIT(A), submitted that the assessee has received advance from customers and also diverted funds to various group companies in the form of share capital and loans and advances. The assessee has not filed any evidence to prove utilization of advances received from the customers for the purpose of business of the assessee. Therefore, the AO has rightly disallowed interest expenses and therefore, their order should be upheld.

11. We have heard the rival submissions and perused the material on record and gone through the orders of the authorities below. The fact borne out from the record indicates that the assessee being in the business of real estate development, has collected advances from customers for sale of flats / commercial complexes in terms of MOU. As per the terms of MOU between the appellant and the customers, there is a provision for payment of interest ranging from 10% to 14% in case of any delay in delivery of flats to the customers. As per the contractual agreement with the customers in terms of MOU, the assessee has paid interest on customers' advances and debited under the head finance charges. The AO has disallowed interest expenses on the ground that the appellant failed to prove utilization of advances received from customers for the purpose of business. The ld. CIT(A) went on a different footing and computed disallowance of interest for diversion of interest-bearing

funds for non-business purpose. We find that the basic business of the assessee is real estate development, and in that process, the assessee collected advances from customers for sale of flats. As per the agreement with the customers, the assessee has paid interest in case of delay in delivery of flats. The assessee had also proved that the funds received from the customers in the form of advances have been utilized for the purpose of business of the assessee. In fact, it is not a case of the AO that the assessee had diverted funds for non-business purposes. Assuming for a moment that loans and advances given to group concerns are diversion of interest-bearing funds, the fact remains that, as the AO himself noted, the group companies of the assessee are also engaged in the business of real estate development and there is a business nexus between the appellant and the group concerns and thus, in our considered opinion, loans and advances given to other group companies can be said to be in the normal course of the business of the assessee and thus, there is a commercial expediency. Therefore, we are of the considered view that the AO erred in disallowing finance charges being interest paid on customers' advances without any valid reasons. The Id. CIT(A), without appreciating the relevant facts, partly confirmed the addition made by the Assessing Officer. Thus, we set aside the order of the Id. CIT(A) and direct the AO to delete the addition sustained by the Id. CIT(A) towards disallowance of finance charges amounting to Rs.83,15,248/-, which was confirmed by the Id. CIT(A).

12. In the result, the appeal filed by the assessee is allowed.

Order pronounced in the Open Court on 4th September, 2024.

Sd/- (LALIET KUMAR) JUDICIAL MEMBER	Sd/- (G. MANJUNATHA) ACCOUNTANT MEMBER
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Hyderabad, dated 4th September, 2024.

TYNM/sps

Copy to:

S.No	Addresses
1	M/s. Kausalya Management Services and Structures Private Limited, No.3-1-188, CVRN Nagar, Karimnagar – 505001.
2	The Deputy Commissioner of Income Tax, Central Circle – 2(3), Hyderabad.
3	PCIT, (Central), Hyderabad / Pr.CIT-Central (Circle), Hyderabad.
4	DR, ITAT Hyderabad Benches
5	Guard File

By Order