

IN THE INCOME TAX APPELLATE TRIBUNAL

"G" BENCH, MUMBAI

BEFORE SHRI AMARJIT SINGH, ACCOUNTANT MEMBER

SHRI SANDEEP SINGH KARHAIL, JUDICIAL MEMBER

ITA No.3406/MUM/2024

(Assessment Year : 2020-21)

Shantiben K Rita,

1601, Laburnum Tower,
SV Road, Goregaon West,
Mumbai - 400104
PAN – AECPR3455A

..... Appellant

v/s

ITO, Ward-41(4)(4),

Kautilya Bhavan, Mumbai
Maharashtra

..... Respondent

Assessee by : Shri Surji D. Chheda, CA

Revenue by : Shri Bhangepatil Pushkaraj Ramesh, Sr.DR

Date of Hearing – 10/10/2024

Date of Order – 06/01/2025

ORDER

PER SANDEEP SINGH KARHAIL, J.M.

The assessee has filed the present appeal against the impugned order dated 29/05/2024, passed under section 250 of the Income Tax Act, 1961 ("the Act") by the learned Commissioner of Income Tax (Appeals), National Faceless Appeal Centre, Delhi ["learned CIT(A)"], for the Assessment Year 2020-21.

2. In this appeal, the assessee has raised the following grounds:

"The learned CIT(A) has erred in law and in facts in confirming the action of AO to make the addition of interest of Rs. 60,53,499/- inspite of the fact that

there is no show cause notice issued for the above addition and failed to appreciate that the addition cannot be made on any issue which is not part of the show cause notice.

2. The learned CIT(A) has erred in law and in facts in rejection of contention of the appellant regarding show cause but failed to appreciate that though show cause notice was issued but no show cause notice was issued to the assessee for above addition of Rs. 50,53,499/- showing the reason that interest expenditure is restricted to an amount of Rs.82,64,051/- and that count only the addition is required to be deleted as addition is against the CBDT instructions.

3. The learned CIT(A) has erred in law and in facts in confirming the action of AO to restrict the interest expenditure to the rate of 5.22% i.e. the average rate at which the interest has been availed by the assessee herself as against actual interest expenditure incurred.

4. The learned CIT(A) has erred in law and in facts to held purely on the assumption and on suspicion basis that the funds taken on interest are being given to related firms at lower interest taken when in fact interest charged to firms at the rate which is higher.

5. The learned CIT(A) has erred in law and in facts to held purely on the assumption and on suspicion basis that the funds taken on interest are being given to family members at lower interest or without interest and claiming business expenditure on such funds is not at all business prudence or business expediency of any nature or at any level.

6. The learned CIT(A) has erred in law and in facts in confirming the action of AO to disallow interest of Rs. 60,53,499/-.

7. The learned CIT(A) has erred in law and in facts in confirming the action of AO to disallow interest in spite of the fact that It has been for earning income from other sources and there is no finding that it is not in accordance with law and in spite of the fact that Section 57 conditions has been fulfilled for allowance of expenditure.

8. The learned CIT(A) has erred in law and in facts in confirming the action of AO to appreciate the facts of the case and has failed to consider the relevant submission as Grot well as submission made during video conference before disallowing the expenditure and made disallowance in a predetermined manner and without application of mind and the learned AO failed to appreciate that addition cannot be made without considering the submission made by the assessee.

9. The learned CIT(A) has erred in law and in facts to held that the appellant assessee has submitted so much, but appellant has not provided any information so at to bring on record the rate of interest at which the funds have been advanced to various related parties but failed to appreciate that issue in show cause notice was notional interest on loan given and not rate of interest and the appellant has not failed in giving any details demanded either to AO or appellate authorities as apparent from orders.

10. The learned CIT(A) has erred in law and in facts in confirming the action of AO in spite of the fact that the learned AO ought to have allowed the interest expenditure when nothing in the reply is found wrong and there is nothing to suggest that interest expenditure has not been spent for earning income from other source."

3. The brief facts of the case are that the assessee is an individual and is a partner in two partnership firms. For the year under consideration, the assessee declared a total income of Rs.11,94,710/- under the head salary, business and profession and income from other sources in her return of income filed on 10.01.2021. The return filed by the assessee was selected for scrutiny primarily to verify the large deduction claimed under section 57 of the Act. In response to the statutory notices issued under section 143(2) and section 142(1) of the Act, the assessee submitted that she had incurred interest expenses amounting to Rs.1,43,17,550/- on loans availed out of which an amount of Rs.1,15,89,437/- was claimed as deduction under section 57 of the Act against the interest income of Rs.1,17,15,147/- declared under the head "*income from other sources*". The balance interest expenditure of Rs.27,28,113/- was claimed by the assessee as a deduction under the head "*income from business and profession*" against the interest income of Rs.32,78,446/- which is an interest income earned on capital from assessee's partnership firm.

4. On perusal of the details filed by the assessee, during the assessment proceedings, it was observed that out of a total loan outstanding as on 31.03.2019 of Rs.17,67,34,180/- an amount of Rs.1,84,18,516/- was taken interest-free and the balance amount of Rs.15,83,15,164/- was received on interest. Further, the interest of Rs.1,43,17,550/- was paid by the assessee

during the year on the net loan amount of Rs.15,83,15,164/- which comes out to 9.04% of the loan amount. It was further observed that out of the total loan given of Rs.22,67,62,305/- as on 31.03.2019, an amount of Rs.24,22,333/- was given interest-free and a balance amount of Rs.22,43,39,972/- was given on interest. Further, an interest of Rs.1,17,15,090/- was earned by the assessee during the year on the loan of Rs.22,43,39,972/-, given during the year, which comes out 5.22% of the loan amount. Since the loan taken by the assessee at the interest rate of 9.04% was given by her to other parties at the average interest rate of 5.22%, the Assessing Officer ("AO") issued show cause notice as to why the minimum interest earned by the assessee from loans given be not calculated at the interest rate of 9.04%, which comes out to Rs.2,02,80,333/- (9.04% of Rs.22,43,39,972/-). In response, the assessee submitted that the actual interest rate differs from the prevailing market rate and is decided upon by various factors like financial ability, negotiable skills etc. The assessee further submitted that a major part of the loan was given at a lower rate of interest as the person was not in a position to pay the higher rate of interest. The AO vide order dated 19.09.2022 passed under section 143(3) r.w.s. 144B of the Act agreed with the contention of the assessee that interest cannot be charged on a notional basis, however restricted the interest expenditure to the rate of 5.22%, i.e., the average rate at which the interest was earned by the assessee. Accordingly, the excess interest expenditure to an extent of Rs.60,53,499/- was disallowed and added to the returned income of the assessee on the basis that the assessee has failed to furnish any business exigency for which the loan was given at a lower rate.

5. The learned CIT(A), vide impugned order, dismissed the grounds raised by the assessee and *inter alia* held that the funds taken on interest are being given by the assessee to family members or related firms at lower rate or without interest which is not at all business prudence or business expediency of any nature or at any level. Accordingly, the learned CIT(A) upheld the disallowance of interest expenditure of Rs.60,53,499/-. Being aggrieved, the assessee is in appeal before us.

6. We have considered the submissions of both sides and perused the material available on record. As evident from the record, the assessee borrowed interest-bearing loan amounting to Rs.15,83,15,164/-, on which she paid an interest of Rs.1,15,89,437/- during the year. It is further evident from the record that the assessee gave interest-bearing loan of Rs.22,43,39,972/-, on which she earned an interest of Rs.1,17,15,090/-. Since, the assessee has declared the interest income of Rs.1,17,15,417/- under the head "*income from other sources*", the amount of Rs.1,15,89,437/- incurred as interest expenditure was claimed as a deduction under section 57(iii) of the Act. As per the assessee, the interest expenditure of Rs.1,15,89,437/- was incurred wholly and exclusively for the purpose of earning the interest income of Rs.1,17,15,147/- and therefore, should be allowed as the deduction under section 57(iii) of the Act while computing the income chargeable under the head "*income from other sources*".

7. On the other hand, as per the Revenue, there is no business exigency for which the loan was given at a lower rate of 5.22% which was availed by the assessee at a rate of 9.04%. Accordingly, the AO restricted the interest

expenditure to a rate of 5.22%. Before proceedings further, it is relevant to note the provisions of section 57(iii) of the Act, which reads as follows: -

"57. The income chargeable under the head "Income from other sources" shall be computed after making the following deductions, namely :—

*(i).....
(ia).....
(ii).....
(ia).....*

(iii) any other expenditure (not being in the nature of capital expenditure) laid out or expended wholly and exclusively for the purpose of making or earning such income."

8. Therefore, under section 57(iii) of the Act, any expenditure which is not in the nature of capital expenditure and has been expended wholly and exclusively for the purpose of earning income chargeable under the head "income from other sources" is allowable as a deduction. In the present case, there is no dispute regarding the nature of expenditure and the Revenue has only disputed that the interest expenditure claimed under the aforesaid section has no nexus for the purpose of earning the interest income. In the present case, it is pertinent to note that no material has been brought on record by the Revenue to show that the loan received by the assessee on which the assessee incurred an interest expenditure of Rs.1,15,89,437/- was utilized for any purpose other than giving the loan to her family members and or related firms. Further, there is no material on record to show that there was any impediment on the assessee to give the money as a loan to her family members or related firms. Thus, there is no material to dispute the fact that the assessee utilized the interest-bearing borrowed funds for advancing the loans to her family members or related firms. In the present case, the

Revenue has emphasized on the aspect of business prudence in advancing the loans to the sister concern at lower rates than the rate at which the funds were borrowed by the assessee. In this regard, it is pertinent to note that it is trite law that the test of commercial expediency/business prudence is required to be judged from the point of view of the businessman and not the Revenue. Therefore, we do not find any basis for restricting the interest expenditure claimed by the assessee under section 57(iii) of the Act.

9. During the hearing, the learned DR placed reliance upon the decision of the Hon'ble Supreme Court in CIT vs. Dr. V.P. Gopinathan, reported in (2001) 248 ITR 449 (SC). From the perusal of the aforesaid decision, we find that in the facts of the case, the taxpayer did not rest its case upon the provisions of section 57(iii) of the Act. Therefore, we find that the reliance placed by the learned DR on the aforesaid decision is completely misplaced.

10. The learned DR also placed reliance upon the decision of the Hon'ble Kerala High Court in Mathew Joseph vs. ACIT, reported in (2017) 87 taxmann.com 317 (Kerala) and the decision of the Hon'ble Jurisdictional High Court in CIT vs. United Wire Ropes Ltd. reported in (1980) 121 ITR 762 (Bom). From the perusal of the aforesaid decisions, it is evident that the loan was given to the taxpayer for a specific purpose for which interest was payable and thus there was no permission by the bankers for the usage of the amount for a purpose other than for which it was given. Accordingly, the Hon'ble Courts denied the deduction claimed under section 57 of the Act. In the present case, no material has been brought on record to show that the assessee was barred by the loan lenders from further transferring the funds

to the family members or related firms on loan. Thus, we are of the considered view that the transaction in this case stands entirely at a different footing and therefore, the aforesaid decisions relied upon by the learned DR are factually distinguishable.

11. Further, the learned DR placed reliance upon the decision of the Hon'ble Karnataka High Court in the case of Karnataka Forest Plantations Corporation Ltd. vs. CIT, reported in (1985) 156 ITR 275 (Karnataka). From the perusal of the aforesaid decision, we find that the Hon'ble Court disallowed the deduction claimed under section 57(iii) of the Act on the basis that the surplus funds arising on account of the amount borrowed by the taxpayer from the State Government and banks from time to time for its business operation got deposited by the assessee in the bank for short period and interest was earned on such deposit. Accordingly, the Hon'ble High Court held that the interest paid by the taxpayer to the bank cannot be considered as incurred wholly and exclusively for the purpose of earning the interest income on surplus funds deposited with the bank. However, in the present case, as noted above, the loan availed by the assessee on interest was used to lend funds to the sister concern on interest and the interest expenditure incurred was claimed as a deduction under section 57(iii) of the Act. Therefore, we are of the considered view that the aforesaid decision is factually distinguishable and is thus not applicable to the present case.

12. Therefore, in view of the facts and circumstances of the present case as noted above, we are considered opinion that the assessee is entitled to claim a deduction under section 57(iii) of the Act in respect of interest expenditure

while computing the income under the head "*income from other sources*". Accordingly, the impugned disallowance made by the AO and upheld by the learned CIT(A) is deleted.

13. Since the relief has been granted to the assessee on merits, the other grounds raised by the assessee are rendered academic and therefore, are left open.

14. In the result, the appeal of the assessee is allowed.

Order pronounced in the open Court on 06/01/2025

Sd/-
AMARJIT SINGH
ACCOUNTANT MEMBER

Sd/-
SANDEEP SINGH KARHAIL
JUDICIAL MEMBER

MUMBAI, DATED: 06/01/2025

Prabhat

Copy of the order forwarded to:

- (1) *The Assessee;*
- (2) *The Revenue;*
- (3) *The PCIT / CIT (Judicial);*
- (4) *The DR, ITAT, Mumbai; and*
- (5) *Guard file.*

By Order

Assistant Registrar
ITAT, Mumbai