

**IN THE INCOME TAX APPELLATE TRIBUNAL
COCHIN BENCH : COCHIN**

**BEFORE SHRI INTURI RAMA RAO, ACCOUNTANT MEMBER
AND
SHRI SOUNDARARAJAN K., JUDICIAL MEMBER**

ITA No. 492/Coch/2025
Assessment Year : 2018-19

Shri Tom George, Travancore Rubber Trading Company, Karimkayam, Mangalamdam, Palakkad – 678 706. PAN: ADBPG5520F	Vs.	The Income Tax Officer, Ward – 1 & TPS, Palakkad.
APPELLANT		RESPONDENT

Assessee by	:	Shri. Padmanathan K V, Advocate
Revenue by	:	Smt. Leena Lal, Snr AR

Date of Hearing	:	04-08-2025
Date of Pronouncement	:	30-10-2025

ORDER

PER SOUNDARARAJAN K., JUDICIAL MEMBER

This is an appeal filed by the assessee challenging the order of the NFAC, Delhi dated 15/05/2025 in respect of the A.Y. 2018-19 and raised the following grounds:

A: The orders of the lower authorities to the extent limiting the deduction of interest paid under section 36(1)(iii) to **Rs.17,51,095/-** is highly unjust, arbitrary and contrary to the facts and the law.

B: The appellant had borrowed **Rs.2,59,51,640/-** from KLM Axiva Finvest, out of which **Rs.1,45,92,464/-** was transferred into the firm's bank account and remaining **Rs.1,13,59,179/-** was directly paid to two sellers from whom the firm has purchased properties. The Assessing Officer as well as the first appellate authority has grossly erred in not accepting **Rs.1,13,59,179/-** as investment in the firm for purpose of deduction under section 36(1)(iii) of the Act.

C: The appellant begs to submit that **Rs.71,27,000/-** and **Rs.42,32,176/-** has been directly paid to Mr. K. Narasingha Reddy and Mr. Venugopal respectively, by the appellant, towards the purchase of properties by the LLP firm. The details of properties purchased are as follows:

Document No. and extent of property	Seller	Buyer	Amount paid by Appellant as partner
Doc 1915/2016 dated 15-07-2016 3.0242 Hectres of land	K. Narasingha Reddy	Kizhakkeparambil Natural Rock Consturctions LLP	Rs.71,27,000/-
Doc. 1916/2016 dated 15-07-2016 1.2186 Hectres of land	V. Venugopal Reddy	Kizhakkeparambil Natural Rock Consturctions LLP	Rs.42,32,176/-
Total			Rs.1,13,59,179/-

The above amounts have been paid by the appellant to the sellers of the property out of commercial expediency. Further, there is a direct nexus between the borrowal of fund by the appellant and its investment in the firm. Hence, interest paid

thereon by the appellant has to be allowed as deduction under section 36(1)(iii) against the remuneration and interest received from the firm.

D: The assessing officer as well as the first appellate authority has grossly erred in restricting the interest under section 36(1)(iii) of the Act to 12%, instead of allowing deduction of the actual interest paid by the appellant to KLM Axiva Finvest. In this regard, the provisions of section 36(1)(iii) read as below:

“Other deductions.

36. (1) The deductions provided for in the following clauses shall be allowed in respect of the matters dealt with therein, in computing the income referred to in section 28-

(iii) the amount of the interest paid in respect of capital borrowed for the purposes of the business or profession.”

E: The appellant begs to submit that amount of deduction under section 36(1)(iii) cannot be restricted to the interest earned from the said investment as held by the Hon'ble Supreme Court of India in **SA builders Ltd vs. CIT reported in 288 ITR 1 (SC)** and followed by Mumbai Bench of Hon'ble Tribunal in **Deepak Nagindas Shah vs ACIT, Circle-19(1), Mumbai ITA 7032/Mum/2019 dated 22-12-2021.**

F: The appellant has borrowed Rs.2,59,51,640/- from KLM Axiva Finvest exclusively for the purpose of investment in the firm. Therefore, the interest paid in respect of capital borrowed of Rs. 60,13,337/-ought to be allowed as deduction against the remuneration and interest received from the firm. Reliance is also placed on decision of Bangalore bench of Hon'ble Tribunal in **Shri Suresh Sriram vs The Income Tax Officer, Ward-3(2)(2), Bangalore in ITA No. 1605/Bang/2019 dated 28-01-2021.**

G: Reliance is also placed on **Santosh Kumar Agrawal v. ACIT in ITA. No. 2925 and 2926/Mum/1997 dated 13.07.2000** and **Ishwardas Satyanarayan Gupta vs ITO, Ward-41(3)(2), Mumbai in ITA 2058/Mum/2023 dated 15-09-2023** wherein Hon'ble Tribunal has held that interest on borrowed capital can be claimed against the remuneration received from firm.

F: The appellant craves leave to add, modify, alter, substitute, withdraw or delete any ground in this appeal.

PRAYER

For these and other submissions to be made at the time of hearing, the Hon'ble Income Tax Appellate Tribunal, Cochin Bench, Cochin maybe pleased to call for records and:

- i. Quash the order passed by the Assessing Officer under section 143(3) of the Act.
- ii. Any other consequential relief as maybe deemed fit and appropriate.

2. The brief facts of the case are that the assessee is a partner in the firm of M/s. Kizhakkeparambil Natural Rock Constructions LLP and filed his return of income on 06/09/2019. Subsequently, the case was selected for limited scrutiny under CASS and notices u/s. 143(2) and 142(1) were issued. The assessee had received a remuneration of Rs. 39,99,577/- from the firm and the interest of Rs. 42,37,308/- from the firm but not reported the said incomes in the return of income filed by him. Thereafter, a show cause notice was issued to the assessee. In response to the show cause notice, the assessee filed a letter on 17/12/2020 and submitted that the assessee had taken a loan from M/s. KLM Axiva Finvest for the purpose of investment in the firm and paid an interest of Rs. 60,13,337/- to the said finance company. The assessee had not submitted any details about the remuneration received from the firm and therefore the same was proposed to be added in the total income of the assessee.

3. In respect of the interest income received from the firm, it comes about Rs. 42,37,308/- which was not offered for taxation, the assessee submitted that the loan was taken from the finance company for the purpose of investment in the firm and paid the interest of Rs. 60,13,337/- and therefore the interest received from the firm is much lesser than the interest paid on the loan obtained from the finance company and therefore the said interest claimed was restricted to the interest income received from

the firm. Thereafter, on further notice, the assessee had furnished the details of the loan taken from the finance company and invested in the firm and the adjustment of the interest. As seen from the submissions made by the assessee, the assessee had taken a loan of Rs. 3 crores on 22/11/2016 from the finance company and out of the said loan amount, a sum of Rs. 1,45,92,462/- was transferred to the firm account and therefore the AO had accepted the said transfer as capital investment and agreed to set off the interest paid on the said loan amount as against the interest income earned from the firm. The AO had restricted the interest rate from 18% to 12% on the ground that the assessee had received interest from the firm at 12%. The balance loan amount of Rs. 1,13,59,176/- were not treated as capital contribution since the said amounts were paid to two individuals and not to the firm and therefore the AO had not agreed to set off the interest paid on the said amount out of the interest income earned from the firm. The AO had restricted the interest paid on the loan taken from the finance company at 12% and granted the deduction and set off the said interest from the interest income earned from the firm and arrived the excess interest expenses claimed at Rs. 24,86,613/-. Finally the AO had added the remuneration received from the firm as well as the excess interest expenses as incomes and assessment has been completed.

4. As against the said order, the assessee filed an appeal before the Ld.CIT(A). The assessee had disputed the inclusion of the remuneration received from the firm as well as the excess interest expenses as income on the ground that the remuneration is an income from business / profession and therefore to earn the said income, the other expenditures incurred by the assessee would be eligible for set off. The assessee further contended that the assessee had taken a loan from the finance company after paying the interest at 18% and invested the said amount in the capital account of the firm and out of the said investments, the assessee had received the interest income from the firm and therefore the interest expenditure should be set off as against income earned by the assessee from the business / profession. The Ld.CIT(A) had not accepted the claim of the assessee since

the remuneration received from the firm is liable to be taxed as per section 28(v) of the Act. The Ld.CIT(A) also observed that the remuneration received from the firm would be exempted in the hands of the partner if the amount is disallowed in the hands of the firm. On the said reasoning, the Ld.CIT(A) had confirmed the assessment made on the remuneration received from the firm. Insofar as the interest issue, the Ld.CIT(A) had confirmed the order of the AO.

5. As against the said order, the assessee is in appeal before this Tribunal.

6. At the time of hearing, the Ld.AR submitted that the AO had failed to consider the fact that the loan amount of Rs. 1,13,59,179/- was paid to two individuals for purchasing the lands in the name of the firm which was later on accounted in the assessee's capital account and therefore the said amount is also eligible to be treated as capital contribution⁴ and consequently the interest paid on the said amount is also eligible for setting off against the interest income earned from the firm. The Ld.AR further submitted that the adoption of rate of interest at 12% as against the 18% paid by the assessee on the loan amount by the AO is also not correct since the section 40(b)(iv) prohibits the payment of the interest by the firm to the partners and not the payment of interest by the assessee on the loan amount borrowed by him and therefore the same yardstick could not be followed for the payment of interest on the loan amount. The Ld.AR further submitted that the AO had failed to consider the fact that the payment of Rs. 1,13,59,179/- was paid to the two sellers while purchasing the agricultural lands in the name of the firm and the said payments were taken into account in the capital account of the assessee and therefore the said payments are also towards the capital contribution and therefore the interest paid on the said amounts are also eligible for set off as against the interest received from the firm. The Ld.AR also relied on the orders of the Coordinate Bench and prayed to allow the appeal.

7. The Ld DR relied on the orders of the lower authorities and prayed to dismiss the appeal.

8. We have heard the arguments of both sides and perused the materials available on record.

9. In the present appeal, we found that the assessee is a partner in a firm and received the remuneration as well as the interest on his capital contributions. To contribute towards the capital, the assessee had also availed the loan from the finance company and paid the interest at 18%. The assessee had received the interest from the firm on his capital account at 12%. The assessee had submitted that the remuneration received by the assessee is also an income from the business or profession and also the interest received from the firm on the capital contribution is also an income from business or profession. As per section 28(v) of the Act, the remuneration received by the assessee from the firm is liable for taxation. The Ld.CIT(A) had considered the said issue and arrived a conclusion that the remuneration received from the firm is exempt in the hands of the assessee if the said amount is disallowed in the hands of the firm. Otherwise, the said remuneration is liable to be taxed under the caption of "Income from business or profession". Before us, the assessee had not raised any grounds with regard to the remuneration received from the firm and therefore we have not expressed any opinion on the said income earned by the assessee from the firm.

10. Insofar as the set off of the interest, it is the case of the assessee that the assessee had obtained loan from the finance company and directly transferred a sum of Rs. 1,45,92,462/- as an investment in the form of capital and the balance Rs. 1,13,59,179/- was paid to the two sellers from whom the firm has purchased properties. The AO had not accepted the payments made to the said two sellers since the loan amount was paid to the two sellers and not directly to the firm's capital account. Before us, the assessee had submitted the sale deed executed with the said two sellers on

15/07/2016 would establishes the fact that the part of the consideration was paid by the assessee by way of cheques on behalf of the firm and the sale deed stood in the name of the firm. The assessee further submitted that the said amount of Rs. 1,13,59,179/- was treated by the firm as the capital contribution and therefore the interest paid on the said amount also to be taken as the interest paid on the contribution of the capital account. From the facts available before us, we are able to ascertain that the assessee out of the loan amount of Rs. 2,59,51,640/-, a sum of Rs. 1,45,92,464/- was directly transferred into the firm's bank account and treated the said as the capital contribution of the assessee. The remaining amount of Rs. 1,13,59,179/- was not treated as capital contribution since the payments were made to some third parties who are not connected with the firm. Even though the payments were made in the name of the third parties, the assessee had paid the amounts out of some urgency and the firm had also taken into account the said amount as the contribution towards the capital account of the assessee. When the said amount was taken as the capital contribution of the assessee, then definitely the payment of interest on the said loan amount also eligible for set off against the interest income earned from the firm. This has to be verified by the AO and thereafter if found that the submissions made by the assessee is correct, then the said amount could be taken as a capital contribution made from the loan amount and therefore the interest paid by the assessee on the said loan amount also eligible for set off as against the interest income earned by the assessee.

11. Further, we are of the view that the interest calculated on the loan amount by the AO at 12% as against the interest at 18% levied by the finance company is also not correct. The Act does not restrict the interest paid on the loan amount equal to the interest earned from the firm on the capital account. Therefore while calculating the interest on the loan amount, we direct the AO to adopt the interest at 18% not at 12% as adopted by the AO in the assessment order.

12. We, therefore, set aside the order of the AO as well as the Ld.CIT(A) insofar as this issue is concerned and remit this issue to the file of the AO for recomputed the income based on the observations given above.

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

Order pronounced in the open court on 30th October, 2025.

Sd/-
(INTURI RAMA RAO)
Accountant Member

Sd/-
(SOUNDARARAJAN K.)
Judicial Member

Cochin,
Dated, the 30th October, 2025
/MS /

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|---------------|---------------------|
| 1. Appellant | 2. Respondent |
| 3. CIT | 4. DR, ITAT, Cochin |
| 5. Guard file | 6. CIT(A) |

By order

Assistant Registrar,
ITAT, Cochin