

**IN THE INCOME TAX APPELLATE TRIBUNAL, 'A' BENCH
MUMBAI**

**BEFORE: SHRI AMIT SHUKLA, JUDICIAL MEMBER
&
SHRI MAKARAND VASANT MAHADEOKAR,
ACCOUNTANT MEMBER**

**ITA No.5901/Mum/2025
(Assessment Year :2017-18)**

Ankur Chandulal Shah 23/A, Atlas Apartment 11, J. Mehta Marg Nepeansea Road Mumbai- 400 006	Vs.	The Asst. Commissioner of Income Tax, Circle-19(1), Mumbai
PAN/GIR No.BAMPS1134C		
(Appellant)	..	(Respondent)

Assessee by	Shri Harsh Kapadia & Shri Ajay Nagpal
Revenue by	Shri Surendra Mohan, Sr. DR
Date of Hearing	21/01/2026
Date of Pronouncement	27/01/2026

आदेश / O R D E R

PER AMIT SHUKLA (J.M):

The aforesaid appeal has been filed by the assessee against the order dated 27/08/2025 passed by the National Faceless Appeal Centre (NFAC), Delhi, for the quantum of assessment framed under section 144 of the Income-tax Act, 1961 for the Assessment Year 2017-18.

2. The solitary grievance raised by the assessee is against the addition of ₹1,06,32,156 made by the Assessing Officer by disallowing deduction of interest expenditure claimed under

the head “Income from Other Sources” under section 57(iii) of the Act.

3. The brief factual matrix qua the issue is that the assessee is an individual and is working as a partner in a partnership firm M/s Creative International. The assessee filed his return of income on 31/10/2017 declaring total income of ₹1,13,74,120. The case of the assessee was selected for scrutiny primarily on the ground of large deduction claimed under section 57. It is an admitted position that there was no response by the assessee to the statutory notices issued by the Assessing Officer during the course of assessment proceedings. Consequently, the Assessing Officer proceeded to frame an ex parte assessment order under section 144, wherein the entire claim of interest expenditure of ₹1,06,32,156 under section 57(iii) was disallowed.

3.1. Before the learned Commissioner of Income-tax (Appeals), it was submitted that during the relevant year the assessee had received interest income from M/s Ariha Diamonds Jewellery Pvt. Ltd. amounting to ₹1,76,81,852, in which the assessee was a Director and shareholder. It was explained that the assessee had advanced loans to the said company and that such advances were funded by loans and advances received by the assessee from his family members and friends, on which the assessee had paid interest aggregating to ₹1,06,30,156. Accordingly, the assessee had offered the net interest income of ₹70,51,426 under the head “Income from Other Sources”. This position was duly reflected

in the computation of total income, wherein the assessee had specifically disclosed interest received from M/s Ariha Diamonds Jewellery Pvt. Ltd. of ₹1,76,81,584 apart from interest received from savings bank accounts. It was thus contended that there existed a direct and proximate nexus between interest income earned and interest expenditure incurred.

3.2. Since the relevant evidences could not be furnished before the Assessing Officer on account of the ex parte nature of the assessment, the assessee filed additional evidences before the learned CIT(A) under Rule 46A, including confirmation letters from M/s Ariha Diamonds Jewellery Pvt. Ltd. as well as from the parties from whom loans and advances had been received and to whom interest had been paid. The learned CIT(A) admitted the additional evidences and called for a remand report from the Assessing Officer. However, despite these evidences and the explanation tendered by the assessee, the learned CIT(A) dismissed the claim of deduction after recording the following findings:

“5.3.4 I have perused the assessment order, submission of the appellant, remand report and judicial precedents on this issue. It is observed that the case of the appellant for the year under consideration has claimed deduction u/s 57(ii) of the Act of Rs. 1,06,32,156/-. Since, the appellant failed to comply with the notices issued by the AO during assessment proceedings, the AO has disallowed the said deduction u/s 57(ii) of the Act and has made addition of Rs. 1,06,32,156/- However, the appellant has claimed that the rejection of claim of the appellant of was incorrect and invalid.

5.3.5. The dispute is regarding allow-ability of expenditure on account of interest paid against interest income earned. The appellant had paid interest of Rs. 1,06,32, 156/ on the borrowed funds. The appellant had also advanced loan to M/s Ariha Diamond Jewellery Pvt. Ltd on which interest income of Rs 1.76.81 852/- had been made. The dispute is whether the interest paid by the assessee can be set off against interest income on loan. The case of the assessee is that while considering allowability of expenditure against income from other sources the entire income has to be considered as a whole and was not necessary to correlate each item of expenditure to income earned. Therefore, if the expenditure had been incurred for earning income from other source and there is no actual earning of income, such expenditure can be allowed against any other item of income from other source.

5.3.6. Here, it is important to note that the deduction u/s 57(iii) of the Act is allowable, if the expenditure (interest paid) was incurred wholly and exclusively to earn interest income. Also, there must be a direct nexus between the borrowing and lending activity. However, in the instant case, the appellant has failed to furnish any documents regarding the usage of the borrowed funds. The burden of proof is on the appellant to prove the nexus between the expenditure (interest paid) and the Income (interest received). The appellant has not provided any evidence such as loan agreements, fund flow details, bank statements which could prove the usage of borrowings. The appellant failed to demonstrate a direct link between borrowed funds and the interest-earning loan. The Hon'ble Supreme Court in the case of CIT v. Rajendra Prasad Moody (SC) has held that "intention to earn income is sufficient. However, this does not override the need to prove a nexus between the expenditure and income. Further, the Hon'ble Court in the case of CIT v. Dalmia Jain & Co. Ltd. has held that "Deduction allowed only when expenditure is directly related to the income earned. Here, it is pertinent to mention that if no proof of use of borrowed funds is given, the deduction could not be allowed even if there was a loss.

5.3.7. In view of the above, it is held that the addition made by the AO of Rs.1,06,32,156/- on account of disallowance of deduction u/s 57(iii) of the Act is upheld. Accordingly, the grounds of appeal are dismissed."

4. We have heard both the parties at length and have carefully perused the relevant findings recorded in the impugned orders. It is an undisputed position that although the assessment order was framed ex parte, during the first appellate proceedings the assessee had placed on record all the relevant documents in support of interest received and interest paid, along with confirmation letters, which were duly admitted by the learned CIT(A), and a remand report was called for from the Assessing Officer.

4.1. From a perusal of these details, it emerges that the assessee had disclosed interest received from M/s Ariha Diamonds Jewellery Pvt. Ltd. amounting to ₹1,76,81,582, which was duly offered as "Income from Other Sources" in the computation of total income, and the same has not been doubted by the Assessing Officer. The interest income arose out of loans and advances given by the assessee to the said company. The assessee had funded these advances through loans and advances received from various persons, on which interest aggregating to ₹1,06,30,156 was paid. The details of such interest payments were furnished before the appellate authority, along with copies of ledger accounts, confirmations and computation of income, which clearly demonstrated that the assessee had reduced the interest paid from the interest received and offered only the net income of ₹71,72,238 as "Income from Other Sources".

4.2. Thus, the factual substratum unmistakably establishes that there existed a direct nexus between interest received and interest paid. Once the Assessing Officer has not doubted

either the genuineness of the interest income received from M/s Ariha Diamonds Jewellery Pvt. Ltd. or the genuineness of the interest expenditure paid by the assessee to various lenders, the denial of deduction under section 57(iii) solely on the premise of alleged lack of nexus becomes unsustainable on both facts and in law. The essence of section 57(iii) lies in whether the expenditure has been laid out wholly and exclusively for the purpose of making or earning income under the head "Income from Other Sources". In the present case, the assessee has demonstrated that the borrowings were utilised for advancing loans to the company from which interest income was earned, and the net interest income has been duly subjected to tax.

4.3. The learned CIT(A) has proceeded to uphold the disallowance on the footing that the assessee failed to furnish documentary proof regarding usage of borrowed funds and failed to demonstrate a direct link between borrowed funds and the interest-earning loan. However, such a conclusion is contrary to the material placed on record, particularly when the confirmations, ledger accounts and computation of income collectively establish a proximate and live nexus between the interest expenditure and the interest income. Moreover, once the additional evidences were admitted and a remand report was called for, and in the absence of any adverse finding by the Assessing Officer in the remand proceedings doubting the genuineness of the transactions, it was not open to the learned CIT(A) to reject the claim merely on conjectural grounds.

4.4. It is also well-settled by the Hon'ble Supreme Court in the case of CIT v. Rajendra Prasad Moody that the expression "for the purpose of making or earning such income" in section 57(iii) does not require that the income should in fact have been earned in the relevant year, and what is relevant is the intention and nexus of the expenditure with the income-earning activity. In the present case, not only is the intention evident, but the income has in fact been earned and taxed. Therefore, the reliance placed by the learned CIT(A) on the said judgment to deny the deduction is wholly misplaced.

In view of the foregoing discussion, we are of the considered opinion that the disallowance of interest expenditure of ₹1,06,32,156 under section 57(iii) is devoid of legal sustainability. Accordingly, the same is directed to be deleted.

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

Order pronounced on 27th January, 2026.

Sd/-
(MAKARAND VASANT
MAHADEOKAR)

ACCOUNTANT MEMBER

Mumbai; Dated 27/01/2026
KARUNA, *sr.ps*

Sd/-
(AMIT SHUKLA)

JUDICIAL 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, Mumbai