

**IN THE INCOME TAX APPELLATE TRIBUNAL
'C' BENCH : BANGALORE**

**BEFORE SHRI ABRAHAM P GEORGE, ACCOUNTANT MEMBER
and
SHRI VIJAY PAL RAO, JUDICIAL MEMBER**

ITA No.1495/Bang/2014
(Assessment year: 2010-11)

Asst. Commissioner of Income-tax,
Circle 4(1)(2),
Bangalore. ... Appellant

Vs.

M/s.Madanapalli Spinning Mills Ltd.,
No.25, I Floor, Mangalam Chambers,
K.P.Road,
Bangalore-560027. ... Respondent
PAN:AABCM4999A

Appellant by: Shri Sunil Kumar Agarwala, JCIT(DR)
Respondent by: Shri Suresh Muthu Krishnan, CA.

Date of hearing : 03/11/2015.
Date of pronouncement: 27/11/2015.

ORDER

Per VIJAY PAL RAO, JM:

This appeal by the revenue is directed against the order dated 13/08/2014 of the CIT(A)-III, Bangalore, for the assessment year 2010-11.

2. The revenue has raised the following grounds:

Page 2 of 8

- 1) *"The order of the learned CIT(A) is opposed to law and facts of the case.*
 - 2) *On the facts and in the circumstances of the case the learned CIT(A) erred in deleting the addition of Rs 49,00,000 being interest on advances made by the assessee to its sister concern without appreciating the fact that the assessee was not able to establish the commercial expediency for advancing interest free loans to its sister concern and was neither able to establish that only non borrowed funds were used for advancing loans by the evidences verified by the AO.*
 - 3) *For these and other grounds that may be urged at the time of hearing, it is prayed that the order of the CIT(A) in so far as it relates to the above grounds may be reversed and that of the Assessing Officer may be restored.*
 - 4) *The appellant craves leave to add, alter, amend and/ or delete any of the grounds mentioned above."*
3. During the course of assessment proceedings, the Assessing Officer (AO) noted that the assessee borrowed secured loan from Bank of India during the previous year by hypothecating plant and machinery, stocks, debtors and mortgage of land and building. The AO further noted that the loan outstanding as on 31/03/2010 was Rs.13.10 crores and the rate of interest was 14% on these secured loans. The AO found that the assessee-company has diverted interest-bearing fund to the tune of Rs.3.5 crores which was borrowed from Bank of India to its sister concern M/s.Vishal Cotspin Ltd., in which the directors of the assessee-company and their family members were the main shareholders. Accordingly, the AO proposed to disallow the

Page 3 of 8

proportionate interest of Rs.49 lakhs being the difference amount in respect of the amount advanced to the sister concern. The assessee contended before the AO that the advances were made as strategic investment and moreover under a merger plan. It was explained before the AO that the assessee-company had entered into a plan for mutual benefit manufacturing and trading activity. Thus, the loan/advances given to the sister were in the normal course of business, though the merger plan with the sister concern was eventually called off. Thus it is manifest from the record that the assessee took the plea that the loan/advance was given to the sister concern for commercial expediency. The AO did not accept the contention of the assessee and disallowed proportionate interest amounting to Rs.49 lakhs by holding that interest-bearing fund was diverted to the related party without getting any business benefits.

4. On appeal, the CIT(A) allowed the claim of the assessee and deleted the disallowance/addition made by the AO by considering the fact that the advance given to the sister concern was given in the financial year 2006-07 and 2007-08 and not during the year under consideration and, therefore, the borrowed fund was not used for the purpose of giving interest-free advance to the sister concern.

Page 4 of 8

5. Before us, learned departmental representative has submitted that the AO has given a finding that interest-bearing fund was diverted to the sister concern and there was no commercial expediency existing for the purpose of transaction of giving interest-free advance whereas the CIT(A) has deleted the disallowance by giving the finding on different grounds and facts. He has relied upon the order of the AO.

6. On the other hand, learned AR of the assessee has submitted that the CIT(A) has given the details of availability of funds as well as recorded the fact that advance was given in the financial years 2006-07 and 2007-08 whereas the interest-bearing loan was taken during the year under consideration. He has supported the finding of the CIT(A).

7. Having considered the rival submissions as well as the relevant material on record, we note that before the AO, the assessee took the plea of commercial expediency in advancing interest-free loan to the sister concern which was not accepted by the AO. The assessee challenged the action of the AO before the CIT(A) and contended that advance was given to the sister concern during the financial year 2006-07 and 2007-08 and not during the year under consideration and therefore, the finding of the AO was alleged to be contrary to the record. Thus it was asserted by the assessee before the CIT(A) that as per annual

Page 5 of 8

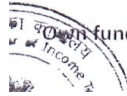
reports, the advance was given in earlier years and not during the year under consideration. The CIT(A) has accepted the claim of the assessee in paras.5 and 6 as under:

"5. I have carefully considered the issue before me. The main contention of the appellant is that the amount of interest free advances were made in the earlier year that is F.Y. 2006-07 and F.Y.2007-08. AR of appellant has furnished copies of the annual reports of the earlier years to establish the factual parameters of the case. AR has thus pointed out that the contentions of the AO that overdraft facility availed by the company in the F.Y 2009-10 has been diverted to M/s.Vishal Cotspin Ltd is factually incorrect. Appellant has also stated that the contention of the AO that there was no commercial benefit in making this interest free advances is also not correct. From the details brought on record by the appellant it is clear that the interest free advances have been made in the F.Y.2006-07 and F.Y 2007-08. This fact is evident from the balance sheet as on 31.03.2010 as outstanding amount from M/s. Vishal Cotspins Ltd for the earlier year is seen. Appellant has furnished the cash flow and funds flow statement in the earlier years to point out these advances are out of the own funds available and not interest bearing funds. The appellant has furnished the following statement to substantiate its case:

Page 6 of 8

Analysis of Cash Flow Statement

Particulars	(Amount in Rs lakhs)		
	2005-06	2006-07	2007-08
Overdraft balance as on 31/03	338.71	535.27	695.39
Increase in Overdraft		196.57	160.11
Incremental Working capital position			
Increase in Trade and Other receivables		515.63	363.09
Increase in Inventories		107.51	11.30
increase/(Decrease) in other payables		431.07	163.23
Net increase		192.08	537.61
Operating Profit available for the year after interest (a)		327.71	177.81
Own funds available for the year without operating profit for the year			
Share Capital		275	275
General Reserve		35.23	-80.44
(b)		310.23	194.56
Share application received ©		167.5	217
funds available (a+b+c)		805.44	233.75



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6. It is clear from a plain reading of the assessment order that these factual parameters have not been taken into account by the AO while framing the assessment order. AO has proceeded on an erroneous premise that the amount of overdraft borrowed from Bank of India during the year at 14% interest has been utilized for the loan to M/s. Vishal Cotspin Ltd. However from the facts brought on record by the appellant it is evident that the loans were outstanding even in earlier years. It can therefore not be stated that the funds borrowed during the year have been diverted to a sister concern for making interest free advances. In my view the addition made is not sustainable as the factual basis relied upon by the AO for making this addition is itself incorrect In view of the facts on record, AO is directed to delete the addition. "

Page 7 of 8

It is manifest from the finding of the CIT(A) that the issue has been decided by considering the fact that the advance was given in the financial years 2006-07 and 2007-08 and not during the year under consideration whereas the interest- bearing loan has been stated to have been taken during the year under consideration. It is pertinent to note that this plea of advancing interest-free loan to the sister concern in the financial years 2006-07 and 2007-08 was not taken before the AO and it appears that it was a fresh plea taken by the assessee before the CIT(A) which was not confronted to the AO for giving his comments and countering the claim of the claim of the assessee. On principle, we do not find any error in the order of the CIT(A) that if the advances were given in the earlier year and the alleged interest-bearing loan was taken during the year under consideration, then no disallowance is called for on account of interest payment. However, since the AO was not given an opportunity to verify these facts, therefore, in the facts of the case and in the interest of justice, we remit this issue to the record of the AO for limited purpose of verifying the facts which have been recorded by the CIT(A) and if the facts are found to be correct, then no disallowance of interest is called for.

Page 8 of 8

8. In the result, the appeal of the revenue is allowed for statistical purposes.

Pronounced in the open court on 27th November, 2015.

sd/-
(Abraham P George)
ACCOUNTANT MEMBER

sd/-
(Vijay Pal Rao)
JUDICIAL MEMBER

eksrinivasulu

Copy to:

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

By order

Assistant Registrar
Income-tax Appellate Tribunal
Bangalore