

IN THE INCOME TAX APPELLATE TRIBUNAL  
SMC "A" BENCH : BANGALORE

BEFORE SMT. ASHA VIJAYARAGHAVAN, JUDICIAL MEMBER

ITA No.357/Bang/2014
Assessment year : 2008-09

Shri Parasmal Dhanraj, Prop. Aluminium Alloys & Allied, No.20, N.R. Road, Bangalore – 560 002. <b>PAN: ACAPD 2130N</b>	Vs.	The Income Tax Officer, Ward 1(4), Bangalore.
APPELLANT		RESPONDENT

Appellant by	:	Shri K. Kiran Kumar, Advocate
Respondent by	:	Dr. P.K. Srihari, Addl. CIT(DR)

Date of hearing	:	22.12.2015
Date of Pronouncement	:	14.01.2016

**ORDER**

This appeal by the assessee is directed against the order dated 09.12.2013 of the CIT(Appeals)-I, Bangalore for the assessment year 2008-09.

2. The appellant, a dealer in aluminium alloys as proprietor of M/s Aluminium Alloys & Allied, filed his return of income for the AY 2008-09 on 30/9/2008, declaring the total income at Rs.4,02,403. Initially the return was processed u/s 143(1) and then selected for scrutiny. In the assessment

completed u/s 143(3) vide order dated 27/12/2011, the total income of the assessee has been determined at Rs.6,18,230 due to the disallowance of an amount of Rs.2,16,187 out of interest paid.

3. Aggrieved, the assessee preferred appeal before the CIT(Appeals). Before the CIT(A), the assessee furnished details of interest paid as under:-

i	Parasmal H.U.F.	Rs. 1,76,130
ii	Smt Posi Bai	Rs. 2,51,235
iii	Smt Lalitha Devi Parasmal	Rs. 57,235
iv	Shri Amit Kumar	Rs. 22,600
	<b>Total</b>	<b>Rs. 5,07,290</b>

4. The CIT(A) observed that as the interest paid/payable exceeds Rs. 10,000, the assessee was liable to deduct tax at source u/s 194A (3) of the Act. However, information available on record revealed that tax was not deducted while making payment or credit of interest in the account of the lenders. Further, it was observed that interest so claimed is still outstanding as on 31.03.2008. In view of the facts stated above, the provisions of section 40(a)(ia) of the Act was attracted and the CIT(A) therefore, proposed to disallow an amount of Rs. 2,91,103 (Rs. 5,07,290 minus Rs. 2,16,187) u/s 40(a) (ia) of the Act.

5. The assessee submitted before the CIT(A) that out of Rs.2,16,187, the assessee has credited interest on loan of Rs.81,231 in his books of accounts in respect of loans given to Sri Dinesh Jain and M/s. Prime Coats as follows:-

SL. No.	Name of Loanee	Amount of Loan	Interest credited in assessee's book	Interest brought to tax by the ITO (@14.50%)
1	Dinesh Jain	Rs.3,50,000	Rs.42,000	Rs.50,750
2	Prime Coats	Rs.3,50,000	Rs.39,231	Rs.50,750
<b>Total</b>		<b>Rs.7,00,000</b>	<b>Rs.81,231</b>	<b>Rs.1,01,500</b>

6. It was therefore submitted before the CIT(A) that the AO has erroneously disallowed Rs.1,01,500 which is a mistake apparent on record and therefore the disallowance was uncalled for.

7. Further, regarding the balance disallowance of Rs.1,14,687 (2,16,187 minus 1,01,500), it was submitted that the assessee had own capital fund available for advancing loans aggregating to Rs.7,90,914 as follows:-

SL. No.	Name of Loanee	Rs.
1	Smt.Arifa Begum	28,554
2	Gyan chand	20,000
3	Mantri Granites	39,000
4	Pratap Corporation	1,21,211
5	Suvarna Distributors	2,96,240
6	Vijay Kumar Goel	2,85,909
<b>Total</b>		<b>7,90,914</b>

8. The assessee submitted that there was a capital balance of Rs.26,75,103 as on 31.3.2008 and hence there was sufficient own capital fund to advance the loans to the above loanees. No part of the borrowed

fund was utilised for the said loan of Rs.7,90,914. Therefore, the disallowance of interest to the extent of Rs.1,14,687 being proportionate interest on the aforesaid loan of Rs.7,90,914 was unjustified. The assessee relied on the decisions of *CIT v. Tin Box Co. (2003) 260 ITR 637 (Del)* and *CIT v. Bharati Televenture Ltd. (2011) 331 ITR 582 (Del)*.

9. Without prejudice to the above contentions, the assessee submitted that interest was not charged on the above loans, since its recovery was doubtful and there was no accrual of interest income and relied on the decision of *DIT v. Brahamputra Capital Financial Services Ltd. [2011] 335 ITR 182 (Del)*.

10. The CIT(A) noted that the source and application of fund from the balance sheet as under:-

Capital account	Rs. 26,75,103
Loan funds	<u>Rs. 48,04,309</u>
Total	<u>Rs. 74,79,413</u>

**Application of funds**

Fixed Assets		1,53,935
Deposits and Advances		24,15,718
Current Assets	62,64,766	
Less-current liabilities	13,55,005	49,09,760
Total		<u>74,79,413</u>

The application of funds includes:

Deposits	1,86,090
Loans & Advances	22,29,628
Closing Stock	39,86,718
Sundry Deposits	18,93,166
DCCIT Transit	2,44,820
CTO Deposits	1,77,963
<b>Total</b>	<b><u>87,18,385</u></b>

11. From the above details, the CIT(Appeals) was of the opinion that admittedly, transactions were made through common pool of funds and hence it was not ascertainable whether loans & Advances were made out of interest free funds only. The CIT(A) observed that the AO disallowed interest of Rs. 2,16,187 on loan & advances given of Rs. 14,90,944. The assessee received Rs.93,557 on loan and advances given to Prime coats, Parswanath Imp-Exp Trading Corporation and Dinesh Jain totaling to Rs. 7,01,115. Thus interest chargeable on Rs. 7,90,944 comes to Rs. 1,14,687, The CIT(A) concluded that loan and advances were given out of interest bearing funds and therefore, disallowance to the extent of Rs. 1,14,687 was confirmed, granting relief of Rs.1,01,500 to the assessee.

12. Aggrieved by the order of CIT(Appeals), the assessee is in appeal before me on the following grounds:-

“1. Since the appellant has given loans of Rs.7,90,914 out of his own capital, the disallowance of interest of Rs.1,14,687 is an error.

2. Since the recovery of loans of Rs.7,90,914 is doubtful, the disallowance of interest of Rs.1,14,687 is an error.”

13. Before me, the Id. counsel for the assessee reiterated the submissions made before the CIT(Appeals). He submitted that the assessee had a capital balance of Rs.26,75,103 as on 31.03.2008. Also, there was sufficient own capital fund on the day on which the loans aggregating to Rs.7,90,914 were lent to the aforesaid loanees. That being, so, the disallowance of interest of Rs. 1,14,687, being proportionate interest on the aforesaid loan of Rs.7,90,914, is unjustified.

14. My attention was drawn to Sampath Iyengar's Law of Income Tax' 11<sup>th</sup> Edition at page 3833, wherein the learned Author A.C. Sampath Iyengar opined that:-

“For the same reason, a presumption appears to be permissible that where an assessee has his own capital as also borrowed funds, the former, rather than the latter could have been utilized for the non-business or personal expenses.”

15. The Id. counsel for the assessee cited an illustration that the Balance Sheet of X as on 31.3.2013 is as follows:-

<b>Capital and liabilities</b>	<b>Rs.</b>	<b>Assets and properties</b>	<b>Rs.</b>
Capital and reserves	10,00,000	Fixed Assets	10,00,000
Borrowing (on interest)	5,00,000	Investment	2,00,000
Current liability	5,00,000	Current assets	8,00,000
<b>Total</b>	<b>20,00,000</b>	<b>Total</b>	<b>20,00,000</b>

16. He submitted that it is apparent that the interest-free funds available with X is Rs, 10,00,000 (being capital and reserve). X decides to advance interest-free loans of Rs.3,00,000 and for that purpose borrows the entire

amount which is interest bearing. On these facts, it was submitted that for allowability of the interest, why should X at all be required to prove the business nexus between the borrowing and its use; because it is obvious that X has adequate 'own resources' (which are free of interest) available with him.

17. In the present case, the proportionate interest on the aforesaid loan of Rs.7,90,914 was Rs.1,14,687. The Id. counsel for the assessee submitted that no part of the borrowed fund was utilized for giving aforesaid loan of Rs.7,90,914. In other words, the assessee had given the aforesaid loans from out of his own capital fund and not from out of the borrowed fund. Moreover, the Id. counsel further submitted that the AO has not found that the borrowed fund has been utilized in giving the aforesaid loans. Therefore, disallowance of interest of Rs. 1,14,687 is, therefore, unjustified. Reliance was placed on the following decisions:-

CIT v. Tin Box Co. (2003) 260 ITR 637 (Del)

CIT v. Bharati Televenture Ltd. (2011) 331 ITR 502

CIT v. Seven Hills Hospitals P. Ltd. [2015] 370 ITR 69 (T&AP)

18. The Id. DR, on the other hand, stated that the CIT(Appeals) has not brought out the facts with respect to reserves and surplus available in order to establish that assessee had enough own funds for giving the loans, except that he has mentioned that the assessee has sufficient reserves, and therefore, this issue has to be further verified by the AO. In these circumstances, I set aside the issue to the file of the Assessing Officer to

examine whether the own capital with the assessee exceeded amount of interest free loans and thereafter decide the issue in the light of the decision in the case of *CIT v. Bharati Televenture Ltd. (2011) 331 ITR 582 (Del)*.

19. With respect to the submission of the assessee that interest has not been charged since the recovery of loans is doubtful, I am of the view that the same has to be examined by the Assessing Officer, who shall verify whether the assessee has taken steps for recovery of loan and whether the loan has become irrecoverable. Accordingly, this issue is set aside to the file of the Assessing Officer for verification as directed above and thereafter decide the issue with respect disallowance of Rs.1,14,687 in the light of the decision in *DIT v. Brahmaputra Capital Financial Services Ltd. [2011] 335 ITR 182 (Del)*.

20. Grounds No.3 to 5 is regarding the disallowance of interest of Rs.5,05,290 u/s. 40(a)(ia) of the Act.

21. The assessee had claimed the following interest amongst other things:-

<b>Sl.No.</b>	<b>Name of Lender</b>	<b>Interest claimed in Rs.</b>
1	Parasmal (HUF)	1,76,130
2	Smt.Posi Bai	2,51,235
3	Smt.Lalitha Devi Parasmal	57,325
4	Sri.Amit Kumar	22,600
	<b>Total</b>	<b>5,05,290</b>

22. The assessee submitted before the CIT(Appeals) that against the interest of Rs.1,76,130 claimed against Parasmal (HUF), the assessee has deducted Rs.14,260 towards TDS. Statement of total income, Form 16A and TDS challans were furnished. Similarly, the assessee submitted that from the material furnished before the CIT(A), viz., ITR-V, Statement of total income, P&L account, capital account and the balance sheet as on 31.3.2008, it was clear that Rs.13,345 has been deducted as TDS. It was hence submitted that the payment of interest to Parasmal (HUF) and Smt. Lalitha Devi Parasmal is not hit by the provisions of section 40(a)(ia).

23. As regards Sri Amit Kumar, it was submitted there was non-deduction of tax at source, since Sri Amit Kumar had furnished Form No.15G and therefore deduction of interest of Rs.22,600 is not hit by the provisions of section 40(a)(ia) of the Act. Reliance was placed on the decision in the case of *Karwat Steel Traders v. ITO*, reported in [2013] 37 taxmann.com 190 (Mum. Trib).

24. The assessee further submitted that all the aforesaid four interest income recipients submitted return of income u/s 139 by declaring interest income and also paid the tax due. The assessee is, thus, not deemed to be in default under the first proviso to sec.201(1) r.w. 2<sup>nd</sup> proviso to sec.40(a)(ia) of the Act and therefore entitled to the allowance of Rs.5,05,290.

25. It was further submitted that though the Finance Act, 2012 inserted the 2<sup>nd</sup> proviso to sec.40(a)(ia) in relation to assessment year 2013-14 and subsequent years, it has to be treated as retrospective with effect from 1<sup>st</sup> April, 2005 i.e. A.Y. 2005-06 and subsequent years because the said amendment is remedial in nature and designed to eliminate unintended consequences which may cause undue hardship to the tax payers and is clarificatory in nature. It was submitted that the main intent of inserting of the section was to make the assessee tax compliant and it was never meant to result into hazardous results, which is also clear from the fact that the Legislation allows deduction of expense in the subsequent years when the tax is deposited. It was further submitted that TDS is only a mode of recovery, which was inserted for early tax collection and once it is recovered, it cannot be taxed again.

26. The assessee referred to the Memorandum explaining the Finance Act, 2012, wherein it was stated as under:-

“In order to rationalize the provisions of disallowance on account of non-deduction of tax from the payments made to a resident payee, it is proposed to amend section 40(a)(ia) to provide that where an assessee makes payment of the nature specified in the said section to a resident payee without deduction of tax and is not deemed to be an assessee in default u/s.201(1) on account of payment of taxes by the payee, then, for the purpose of allowing deduction of such, it shall be deemed that the assessee has deducted and paid the tax on such sum on the date of furnishing of return of income by the resident payee”.

27. It was the assessee's submission that from the language used in the Memorandum explaining the Finance Act, 2012, that it has been introduced as a remedy for the malady being faced by the tax payers and is clarificatory in nature. The provision is not intended for punitive action on non-compliance and should be treated as with retrospective effect. Reliance was placed on the decision in the case of *CIT v. Alom Extrusions Ltd.* [(2009) 319 ITR 306 (SC)].

28. The CIT(Appeals) has at page 11 to 14 of the impugned order discussed the issue of disallowance of interest u/s. 40(a)(ia) in respect of interest payments in the case of Parasmal (HUF), Smt. Lalitha Devi Parasmal, Sri Amit Kumar and Smt. Posi Bai and the CIT(A) has confirmed the disallowance of interest and enhancement of income of Rs.5,05,290 u/s. 40(a)(ia) of the Act.

29. Aggrieved, the assessee is in appeal before me.

30. The Id. counsel for the assessee reiterated the submissions made before the CIT(Appeals). On the other hand, the Id. DR stated that details of TDS payments filed before us has not been placed before the AO and the AO has to necessarily verify whether TDS has been deducted with respect to interest paid. In these circumstances, it was prayed that the matter be set aside to the file of the AO for verification.

31. I have heard both the parties and perused the material on record. I am of the opinion that the issue requires verification by the AO. Accordingly, the issue is set aside to the file of the Assessing Officer, who shall verify the fact of TDS payments in the case of Parasmal HUF, Smt. Posi Bai and Smt. Lalitha Devi Parasmal and Form 15G furnished by the lender, Shri Amit Kumar Jain claiming non-deduction of TDS. The Assessing Officer shall decide the issue afresh in accordance with law.

32. In the result, the appeal is allowed for statistical purposes.

Pronounced in the open court on this 14<sup>th</sup> day of January, 2016.

Sd/-

(ASHA VIJAYARAGHAVAN )  
Judicial Member

Bangalore,  
Dated, the 14<sup>th</sup> January, 2016.

/D S/

Copy to:

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

By order

Assistant Registrar,  
ITAT, Bangalore.