

**आयकर अपीलीय अधिकरण "E" न्यायपीठ मुंबई में।**

**IN THE INCOME TAX APPELLATE TRIBUNAL "E" BENCH, MUMBAI**

**BEFORE SHRI C.N. PRASAD, JUDICIAL MEMBER  
AND SHRI RAMIT KOCHAR, ACCOUNTANT MEMBER**

आयकर अपील सं./I.T.A. No.1430/Mum/2014

(निर्धारण वर्ष / Assessment Year : 2010-11)

Sushil Kumar Beniprasad Goenka, Plot No. 6, F-11/12, WICEL, Opp Seepz, MIDC, Andheri (E), Mumbai - 400 093.	<b>बनाम/</b> v.	Income Tax Officer - 14(2)(2), Mumbai.
स्थायी लेखा सं./PAN : AADPG 0850 B		
(अपीलार्थी / <b>Appellant</b> )	..	(प्रत्यर्थी / <b>Respondent</b> )

Assessee by	Shri Rishabh Chaturvedi
Revenue by :	Ms. Pooja Swaroop (D.R.)

सुनवाई की तारीख / **Date of Hearing** : 23-08-2016

घोषणा की तारीख / **Date of Pronouncement** : 11-11-2016

**आदेश / ORDER**

**PER RAMIT KOCHAR, Accountant Member**

This appeal, filed by the assessee, being ITA No. 1430/Mum/2014, is directed against the appellate order dated 7<sup>th</sup> October, 2013 passed by learned Commissioner of Income Tax (Appeals)- 25, Mumbai (hereinafter called "the CIT(A)"), for the assessment year 2010-11, the appellate proceedings before the learned CIT(A) arising from the assessment order dated 17<sup>th</sup> December, 2012 passed by the learned Assessing Officer (hereinafter called "the AO") u/s 143(3) r.w.s. 147 of the Income-tax Act, 1961 (Hereinafter called "the Act").

2. The grounds of appeal raised by the assessee in the memo of appeal filed with the Income Tax Appellate Tribunal, Mumbai (hereinafter called "the Tribunal") read as under:-

"1. Learned Commissioner of Income Tax (Appeal)-25, on the facts and circumstances of the case and in law, has erred in disallowing interest expense of Rs. 10,27,507/-.

The Appellant respectfully submits that CIT(A) ought to have considered that interest expense was incurred to earn interest income on capital balance in the firm which is taxable as business income and ought to have ignored Appellant's mistake of claiming interest expense as loss under the head "Income from other sources" instead of "Business Loss" as there is no estoppel against law, particularly when the total income, as returned, remains the same."

3. The Brief facts of the case are that the return of income declaring total income of Rs. 19,63,290/- was filed by the assessee on 14<sup>th</sup> October, 2010 which was processed u/s 143(1) of the Act. The case was reopened u/s 148 of the Act for the reasons recorded as under:-

"On perusal of the case records, it is seen that assessee has shown salary income of Rs.30,00,000/- after claiming deduction u/s 10 and interest income of Rs. 1,08,297/-, the assessee claimed deduction of Rs.10,27,507/- on account of interest payment against the salary income and interest income.

It may be noted that the only allowable deduction out of salary income are professional tax and entertainment allowances. The deduction of interest payment claimed by the assessee out of the salary income is not allowable under the Income tax Act and interest payment claimed against the interest income are allowable only if the said expenses are incurred for the purpose of making or earning such income as per the section u/s 57 of the I.T. Act, 1961".

Notice u/s 148 of the Act was issued and served on the assessee and in reply the assessee stated that the original return of income filed may be treated as having filed in response to notice u/s 148 of the Act. The case was reopened to disallow the claim of deduction of Rs. 10,27,507/- on account of interest payment to LIC of India against salary income and interest income and the assessee has submitted as under:-

- “1. I have borrowed from LIC and have paid interest of Rs. 10,27,507/- during the year ended 31.3.2010.
2. Above borrowed funds have been utilized by me in investing in Systematic Exports, a firm in which I am a partner.
3. The purpose of giving above loan was to earn interest. However, unfortunately, due to losses, Systematic Exports has been unable to pay any interest.
4. If Systematic Exports had earned profits and was in a position to pay interest to me, I would have shown the same as my Business Income as per 28(v) of the said Act. The interest paid by me on borrowings utilized with the purpose of earning interest is a deductible business expenditure under section 36,37 and other relevant provisions of the said Act.
5. I have, by mistake, claimed the said interest as deduction from income from other sources. By this letter, I wish to correct this mistake and claim the above interest expense as a business expenditure.
6. As a result, due to interest expense and no corresponding interest income which would have been liable to tax as business income (investment as capital in partnership firm to earn interest u/s 28(iv)), I have incurred the loss of Rs.10,27,507/- under the head "profits and gains of business or profession.
7. My income from other sources stand corrected to Rs. 1,08,297/- instead of loss of Rs. 9,19,210/-.

8. After setting off of business loss against income from other heads, viz; salary income, income from capital gain and income from other sources, my total income shall remain same as my returned income.”

It was observed by the A.O. that the assessee has taken loan to invest in partnership firm. The share of profit from the partnership is exempt u/s 10(2A) of the Act. The assessee's contention that the loan amount was invested in the partnership firm with the intention of earning interest was not acceptable to the A.O. The A.O. observed that share of profit from capital contribution in the partnership firm is exempt from tax u/s 10(2A) of the Act . Hence, the contention of the assessee that had there been profit in the partnership firm, the assessee would have received interest was not acceptable/teneble. The disallowance u/s 14A of the Act was not worked out by the assessee as observed by the AO. The assessee had made investment in the capital of partnership firm out of loan received from LIC and the assessee has not paid the interest on loan taken for the purposes of earning interest as no interest was received from partnership firm. The A.O. accordingly computed the income of the assessee by disallowing the interest paid to LIC amounting to Rs. 10,27,507/- vide assessment order dated 17<sup>th</sup> December, 2012 passed u/s 143(3) r.w.s. 147 of the Act.

4. Aggrieved by the assessment order dated 17.12.2012 passed by the A.O. u/s 143(3) of the Act read with Section 147 of the Act, the assessee filed first appeal before the ld. CIT(A).

5. Before the ld. CIT(A) , the assessee reiterated the submission what were made before the A.O. and submitted that he had borrowed funds from LIC and paid interest of Rs. 10,27,507/- during the year and this money had been utilized for investing in the capital of Systematic Exports in which the assessee is a partner. The assessee credited this borrowed fund in his capital account in the books of the firm and interest is allowable to partners in terms

of partnership deed of the firm. The assessee submitted copy of bank book, bank statements, capital account, partnership deed, balance sheet and income tax return of the firm etc. before the learned CIT(A). The learned CIT(A) observed that the assessee has availed loan from LIC on which interest of Rs. 10,27,507/- was paid by the assessee which was set off against income from other sources and salary income. The assessee had claimed to have invested loan proceeds from LIC in the capital of the firm M/s Systematic Exports for the purposes of earning interest as per contentions of the assessee. The learned CIT(A) observed from the balance sheet of the firm M/s Systematic Exports that the assessee had opening outstanding capital at Rs. 4,82,079/-, additions made during the year at Rs.67,786/-, withdrawals during the year at Rs.5,33,834/-, share of loss at Rs. 5,29,619/-, and closing balance in negative at Rs. 5,13,588/-. The assessee was entitled to 15% share in the capital of firm and his capital at the end of year was negative, as against total capital of the firm at Rs.346.05 lakhs. The ld. CIT(A) referred to Clause 8 of Partnership Deed which reads as under:-

*"The capital of the partnership shall be brought in by the partners as and when required for the business in the manner as mutually agreed 'upon between the parties referred hereto, and the partners may be paid interest, at a rate, on their Capital as may be mutually agreed upon from time to time."*

Thus, it was observed by the ld. CIT(A) that the intention of the assessee in taking loan from LIC was not to invest in capital of the firm with the sole intention of earning interest from the firm. The learned CIT(A) observed that the assessee failed to show any nexus with the loans taken and payments made to the firm except a stray incident instance which is not sufficient to justify the interest payment of an amount as high as Rs.10,27,507/- on such loans taken. There is no evidence to prove that the assessee's sole intention was to earn interest on capital employed in the firm as against share in profits which is exempted u/s 10(2A) of the Act. The capital of the assessee

was not just sufficient even for his 15% share in the firm and is in negative was the observation of learned CIT(A). The ld. CIT(A) accordingly concluded that the assessee has grossly failed to justify that the interest paid of Rs. 10,27,507/- had nexus with any business purposes of the assessee and it is an afterthought just to avoid the payment of taxes. Thus, the ld. CIT(A) upheld the order of the A.O. vide appellate order dated 07-10-20113 passed by learned CIT(A).

6. Aggrieved by the appellate order dated 07-10-2013 passed by the ld. CIT(A), the assessee filed appeal before the Tribunal.

7. The ld. Counsel for the assessee submitted that the assessee has availed LIC loan and interest is paid on the said loan. The assessee has invested the said loan in partnership firm Systematic Exports in which the assessee is partner and the assessee would have earned interest had there been profits, by relying on clause 8 of the partnership deed. The assessee has claimed the interest paid of Rs. 10,27,507/- by setting off against income from other sources and salary income.

8. The ld. D.R. submitted that the A.O. has invoked the provisions of section 14A of the Act. The interest paid by the assessee on LIC loan which was invested in partnership firm was rightly disallowed by the A.O. as the share of profit from partnership firm is exempt from tax u/s 10(2A) of the Act. The learned DR relied on the orders of the learned CIT(A).

9. In the rejoinder, the ld. Counsel submitted that interest income on capital of partnership firm is taxable u/s 28(v) of the Act and hence interest should be allowed as deduction / set off against income from other sources and salary. It was submitted that had there been profits, the partnership firm

Systematic Exports in which the assessee was partner would have given interest on the investment in the capital by the assessee.

10. We have heard the rival contentions and also perused the material available on record. We have observed that the assessee is partner in firm M/s Systematic Exports. The assessee has availed loan from LIC and paid interest of Rs.10,27,507/- which was claimed as an expense under the head 'profit and gain from business or profession'. The assessee has set off the said interest paid to LIC against income from other sources and salary income. The assessee has income from other sources to the tune of Rs. 1,18,297/- and salary income of Rs. 9,19,210/-. Before proceeding further, we would like to state that losses under the head 'Profit and gain from business or profession' are not allowed to be set off against salary income in view of provisions of Section 71(2A) of the Act which was inserted by Finance Act, 2004, w.e.f. 01-04-2005. The assessee has stated to have invested LIC Loan in the capital of the partnership firm M/s Systematic Exports but on careful perusal of the ledger extracts submitted by the assessee in the paper book filed before the tribunal, we have observed that the assessee has invested only Rs. 10,00,000/- in the capital of partnership firm Systematic Exports on 17/10/2008 (pb/page 4 & 11) , while the total loan from LIC outstanding in the books of the assessee as on 31-03-2009 was Rs. 1,19,11,688.68 (pb/page 7 ) which was raised in financial year 2008-09, including interest for financial year 2008-09. We have observed from perusal of Canara Bank Book submitted by the assessee vide paper book/page 4 that the assessee has made payment of Rs. 25,00,000/- on 10-10-2008 to City Apparels vide cheque no. 153747 , Rs. 43,00,000/- to City Apparels vide cheque no. 153748 dated 14-10-2008, Rs.15,00,000/- to Sushil Goenka HUF vide cheque 153751 on 15-10-2008, Rs. 20,00,000/- to City Apparels vide cheque no. 153752 on 17-10-2008 and also payment of Rs. 10,00,000/- to Systematic Exports vide cheque no. 153753 dated 17-10-2008. Thus, the

assessee has invested only Rs. 10 lacs in the firm Systematic Exports out of Rs.1.19 crore of LIC loan (inclusive of interest for financial year 2008-09) outstanding as at 31-03-2009. Thus, there is a perversity in contention of the assessee and findings of the authorities below as the assessee has not invested the entire proceeds of the LIC loan of Rs.1.19 crores (inclusive of interest for 2008-09) in the firm Systematic Exports but for Rs. 10.0 lacs as set out above. The capital account of the assessee in books of Systematic Exports also confirms the same. The balance outstanding in the capital account of the assessee with Systematic Exports is negative as brought out in the learned CIT(A) orders from the balance sheet of the firm M/s Systematic Exports that the assessee had opening outstanding capital at Rs. 4,82,079/-, additions made during the year at Rs.67,786/-, withdrawals during the year at Rs.5,33,834/-, share of loss at Rs. 5,29,619/-, and closing balance in negative at Rs. 5,13,588/-. The assessee was entitled to 15% share in the capital of firm and his capital at the end of year was negative, as against total capital of the firm at Rs.346.05 lakhs. The assessee could not rebut said findings before the Tribunal rather the audited financial statements of Systematic Exports confirms the finding of learned CIT(A) page 21/paper book filed with the Tribunal. There is no binding stipulation in the partnership deed w.r.t. payment of interest on capital contributed by partners rather there is a general clause in partnership deed vide clause 8 which reads as under :

*"The capital of the partnership shall be brought in by the partners as and when required for the business in the manner as mutually agreed upon between the parties referred hereto, and the partners may be paid interest, at a rate, on their Capital as may be mutually agreed upon from time to time."*

There is a general clause in the partnership deed vide clause 8 of partnership deed that the interest may be paid to the partners on the capital contributed to the partnership firm by the partners as mutually agreed by the partners.

No doubt, the interest due to or received by partner on capital contributed by partners in partnership firm is assessed to tax as business income u/s 28(v) of the Act in the hands of the partner but the assessee could not show that the partners have in-fact agreed to pay interest on their capital contributed in the partnership firm M/s Systematic Exports during the impugned assessment year and a valid and legal binding obligation is cast on the partnership firm M/s Systematic Exports to pay interest on capital specifically to the partners in presenti during the impugned assessment year . The assessee's had taken a contention that had there been any profits in Systematic Export, the assessee would have received interest from the partnership firm need verification from the actual conduct of Systematic Exports over the years to prove that the firm Systematic Exports in fact paid interest on capital contributed by the partners when there were profits in the said firm . The share of profits on the capital contributed by the assessee with the partnership firm M/s Systematic Exports , are exempt from tax u/s. 10(2A) of the Act. Thus, necessarily the expenses incurred in relation to earning of the income which does not form part of total income, has to be disallowed as per provisions and mandate of Section 14A of the Act unless it is shown that the interest is paid / payable on the capital contributed by the partner in the firm Systematic Exports which interest is chargeable to tax u/s 28(v) of the Act . Considering the peculiar facts and circumstances of the case, interest of justice will be best served if the matter is set aside and restored to the file of the AO for fresh determination of the issue on merits in accordance with law while also keeping in view our above stated observations in this order. The assessee shall be allowed to file relevant evidences / explanations in his defense. Needless to say proper and adequate opportunity of being heard shall be granted to the assessee in accordance with principles of natural justice. The appeal of the assessee is allowed for statistical purposes. We order accordingly.

9. In the result, appeal filed by the assessee in ITA No. 1430/Mum/2014 for the assessment year 2010-11 is allowed for statistical purposes.

Order pronounced in the open court on 11<sup>th</sup> November , 2016.

आदेश की घोषणा खुले न्यायालय में दिनांक: 11-11-2016 को की गई ।

Sd/-  
(C.N. PRASAD)  
JUDICIAL MEMBER

sd/-  
(RAMIT KOCHAR)  
ACCOUNTANT MEMBER

मुंबई Mumbai; दिनांक Dated 11-11-2016

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व.नि.स./ R.K., Ex. Sr. PS

**आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :**

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent.
3. आयकर आयुक्त(अपील) / The CIT(A)- concerned, Mumbai
4. आयकर आयुक्त / CIT- Concerned, Mumbai
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, मुंबई / DR, ITAT, Mumbai "E" Bench
6. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER,

सत्यापित प्रति //True Copy//

उप/सहायक पंजीकार (Dy./Asstt. Registrar)  
आयकर अपीलीय अधिकरण, मुंबई/ ITAT, Mumbai