

आयकर अपीलिय अधिकरण, अहमदाबाद न्यायपीठ "ए", अहमदाबाद ।
IN THE INCOME TAX APPELLATE TRIBUNAL
" A " BENCH, AHMEDABAD

BEFORE SMT.ANNAPURNA GUPTA, ACCOUNTANT MEMBER
AND
MS. MADHUMITA ROY, JUDICIAL MEMBER

ITA No.429/Ahd/2018
Assessment Year : 2013-14

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| Shri Girishbhai Vadilal Shah 139, V.R. Shah Smruti Shikshan Mandir Nr.Dharnidhar Derasar Vasna Ahmedabad-380 007 | Vs | The Dy.CIT Circle-5(2) Ahmedabad |
| PAN: ABJPS 3102 P | | |

| अपीलार्थी/ (Appellant) | प्रत्यर्थी/ (Respondent) |
|------------------------|------------------------------|
| Assessee by : | Shri Jaimin Shah, AR |
| Revenue by : | Ms.Saumya Pandey Jain, Sr.DR |

सुनवाई की तारीख/Date of Hearing : 05/03/2024
घोषणा की तारीख /Date of Pronouncement: 15/03/2024

आदेश/ORDER

PER ANNAPURNA GUPTA, ACCOUNTANT MEMBER:

This appeal filed by the Assessee is directed against the order of Learned Commissioner of Income-Tax (Appeals), Ahmedabad-5 [hereinafter referred to as "Ld. CIT(A)" for short] dated 08/12/2017 passed for Assessment Year (AY) 2013-14.

2. The assessee has raised the following grounds of appeal:

"1. That the LD. A.O. has erred both in law and on facts while disallowing of interest expenses of Rs.54,32,948/- of the I.T. Act. 1961. Hence, it is required to be deleted.

2. That the Ld. A.O. has without considering the facts and circumstances of the case disallowed interest expenses of Rs.54,32,948/- is against the principal of natural justice and therefore it requires to be deleted.

3. That the Ld. A.O. has disallowed the notional interest of Rs.54,32,948/- without considering the facts that the advances given to the persons are paying tax at maximum marginal rate and therefore there is no any question of tax evasion. However the disallowances made without considering the above facts and circumstances which requires to be deleted.

4. That the assessee has not concealed or suppressed any particulars of income as per explanation-1 to section 271(1)(c) and as such the penalty and interest u / s 234A, 234B and 234C may please be deleted."

3. The solitary issue in the present appeal relates to the disallowance of claim of interest expenses u/s.57(iii) of the Income Tax Act, 1961 (hereinafter referred to as "the Act" for short) amounting to Rs.54,32,948/-.

The orders of the authorities below reveal the facts of the case as that the assessee had shown interest income of Rs.1,08,39,837/- under the head "income from other sources" and claimed expenses against the same of Rs.1,08,52,717/-. Thus, the assessee has returned the loss of Rs.12,880/- under the head "income from other sources". Out of this claim of Rs.1.08 crores of interest expenses the Assessing Officer disallowed expenses to the tune of Rs.54,32,948/- which were in relation to loans taken by the assessee on which the rate of interest paid was found to be more than the rate at which the loans were advanced. The Assessing Officer noted that while the assessee had charged interest @12%, the same had been advanced by charging lower rate of interest, i.e. ranging from 6% to 10% and the difference accordingly was worked out and was disallowed in terms of

section 57(iii) of the Act. The working of the disallowance is narrated at Paragraph No.5.10 of the assessment order as under:

"5.10 In view of the above facts and the legal discussion made, the interest expenses claimed by the assessee u/s.57(iii) are not allowable to the extent they are attributable to the lower interest charged by the assessee than 12% pa on the advanced made. The same have been worked out in the following manner:

| Sr.No. | Name | Interest | Rate of interest | Amt. of interest chargeable @ 12% |
|--------|--|----------|------------------|-----------------------------------|
| 1. | Bhaumik R.APatel | 434795 | 9 | 579727 |
| 2. | M. Enterprise | 540000 | 6 | 1080000 |
| 3. | P.C. Trading | 156164 | 6 | 312328 |
| 4. | Saurin & Co. | 31233 | 12 | 31233 |
| 5. | Shree Sehaj Alloy Pvt.Ltd. | 450000 | 9 | 600000 |
| 6. | Sh. V.R. Shah – Smruti Adarsh Education Trust | 2067333 | 9 | 2756444 |
| 7. | Vimlachal Print & Pack Pvt.Ltd. | 889315 | 10 | 1067178 |
| 8. | Harmish G. Shah (Closing Balance as on 31.03.13 Rs.46155500/-) | 0 | 0 | 5601756 |
| | Total | 7369718 | | 12028666" |

4. The same was upheld by the Ld.CIT(A).

5. We have heard both the parties and have also gone through the orders of the authorities below. After careful consideration of all of the above, we hold that the disallowance made of interest in the present case u/s.57(iii) of the Act is not sustainable. The reason for the same is simple.

As is evident from the order of the AO reproduced above, he has disallowed that portion of the interest expense incurred on loans taken which was in excess of the interest charged on loans given by the assessee. Which means that in sum and substance he accepted the usage of interest bearing funds for earning interest income when he allowed that portion of interest expense which was in parity with the interest charged by the assessee on loans/advances given. Having accepted this fact therefore the AO was precluded from making any disallowance of interest u/s 57(iii) of the Act since the only requirement to be fulfilled for claiming expenses under the said section is that they must have been incurred wholly and exclusively for the purpose of earning income from other sources. What is relevant therefore is only the nexus of expenditure for earning income and the quantum of expenditure incurred therefore is of no consequence.

The Assessing Officer in his order passed u/s.143(3) of the Act himself interprets the provisions of section 57(iii) of the Act and notes that for allowability of expenses under the said section, the nexus of the expenditure with the earning of income is essential conditions to be fulfilled as reproduced at Paragraph No.5.5 of his order as under:

“5.5 From the above, provisions, it can be appreciated that deduction from interest income is allowable u/s.57(iii) only. An analysis of this sub- section would show that in computing the income under this head the assessee is entitled to deduction in respect of the expenditure incurred solely for the purpose of earning such income, provided the expenditure is not of a capital nature and does not include any personal expenses incurred by the assessee. In other words, before this provision could apply, the following conditions must be fulfilled:

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| (i) | <i>the expenditure must have been incurred solely and exclusively for the purpose of earning income or making profit;</i> |
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|-------|---|
| (ii) | <i>the expenditure should not be in the nature of a capital expenditure;</i> |
| (iii) | <i>the amount in question should not be in the nature of personal expenses of the assessee;</i> |
| (iv) | <i>that the expenditure should be incurred in the accounting year; and</i> |
| (v) | <i>There must be a clear nexus between the expenditure incurred and the income sought to be earned."</i> |

5.1 Therefore, clearly the disallowance made u/s 57(iii) of the Act of Rs.54,32,948/- is contrary to law as interpreted by the Revenue authorities themselves. Moreover, we have noted that the Revenue authorities have also misinterpreted the provision of section 57(iii) of the Act by stating that expenses under the section can be allowed only if income is earned from the incurrance of the said expense, and the term income means profit earned. The Revenue authorities have made the disallowance in the present case noting that assessee had made losses and therefore as earned no income. This finding of the Assessing Officer is at Paragraph No.5.6 of his order reads as under:

"5.6. Now coming to the reply of the assessee and the contention that primary motive of incurring interest by the assessee is to earn income falling under the head 'income from other sources'. This contention of the assessee, however is devoid of substance, in view of the fact that the amount of interest paid by the assessee is higher than the amount of interest received. Had the primary motive of the assessee been to earn interest, no loss would have been possible on this account."

5.2. The Ld.CIT(A) has confirmed this finding of the Assessing Officer.

5.3. This basis of the Assessing Officer is completely devoid of any merits, what the section requires is that expenses must have been incurred for the purpose of earning income to be eligible to claim the same against the said

income. There is no question of interpreting the term “income as profits”. The moment expenditure has been incurred for earning income, the expenditure incurred for the same qualifies for deduction u/s.54(iii) of the Act. In the present case, it is not disputed that the assessee has earned interest income of Rs.1,08,39,837/-. Therefore, the Assessing Officer’s finding that there is no income is factually incorrect and this basis of the Assessing Officer is, therefore, for denying the assessee’s claim of expenditure u/s.57(iii) of the Act is liable to be quashed.

Besides, there is again a basic fallacy in the reasoning as above of the Revenue authorities since as noted above by us they themselves have allowed a portion of the interest expense disallowing only the excess in comparison to the interest income earned. If no income was earned by the assessee, as is the case of the Revenue authorities, then the entire interest expense ought to have been disallowed.

Further, we find that the Assessing Officer mentions at Paragraph No.5.8 in his order that the assessee claimed to have been interest from his OD account with Kalupur Bank for lending money and receiving money and thus establishing nexus between the funds borrowed on interest and utilized for making advances for earning interest thereon for claiming interest expenses against the interest income earned. We find that the Assessing Officer has dismissed this contention of the assessee stating that there ought to be a clear nexus between the expenditure incurred and the income earned as observed by the Hon’ble Apex Court in its decision reported at **110 ITR 664**. The Assessing Officer has not stated as to how in the light of the facts stated by the assessee, the nexus was not established, he

has just summarily dismissed the contention of the assessee. In the absence of the Assessing Officer pointing out as to how despite the assessee's explanation, there was no nexus between the interest bearing-funds and their utilization for making advances for earning interest income, no disallowance u/s 57(iii) of the Act was tenable.

In view of the above, we hold that the disallowance of interest expenses u/s.57(iii) of the Act confirmed by the Ld.CIT(A) was incorrect and unwarranted. The same is, therefore, directed to be deleted. Thus, grounds of appeal of the assessee are allowed.

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

Order pronounced in the Court on 15th March, 2024 at Ahmedabad.

Sd/-
(MADHUMITHA ROY)
JUDICIAL MEMBER

Sd/-
(ANNAPURNA GUPTA)
ACCOUNTANT MEMBER

Ahmedabad, Dated 15/03/2024

टी.सी.नायर, व.नि.स।T.C. NAIR, Sr. PS

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

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent.
3. संबंधित आयकर आयुक्त / Concerned CIT
4. आयकर आयुक्त (अपील)/ The CIT(A), Ahmedabad-5
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण , राजकोट/DR, ITAT, Ahmedabad,
6. गार्ड फाईल /Guard file.

आदेशानुसार/ BY ORDER,

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सहायक पंजीकार (Asstt. Registrar)
आयकर अपीलीय अधिकरण, ITAT, Ahmedabad