

## HC disallows interest on borrowings as assessee artificially borrowed its owned funds through a circuitous route

**Summary – The High Court of Karnataka in a recent case of Bellary Steels and Alloys Ltd., (the Assessee) held that where assessee had invested its borrowed fund in a company but said company advanced said sum to another company which again invested said sum in assessee company, interest on borrowed capital need disallowance as borrowed fund was utilized for non-business purposes**

### Facts

- Assessee had invested borrowed sum in a company 'P' for the purpose of generation of electricity and supplied it to the assessee-company.
- Said 'P' had neither generated electricity nor supplied it to the company and siphoned off part of said sum to 'S' another company as unsecured loans and that 'S' had pumped in the said money into the assessee towards purchase of shares.
- The Assessing Officer held that there had been conjoint action by participating companies to siphon off the interest bearing borrowed funds for non-business purpose and, therefore, he held that the amount of the borrowed funds from banks and financial institutions was diverted and invested by the assessee in various associated companies and it was not a genuine business transaction and therefore, the proportionate interest at the prevailing rates paid by the companies was disallowed and added back to the total income of the assessee.
- The Commissioner (Appeals) after re-appreciating the entire material on record, confirmed the said findings.
- The Tribunal was of the view that there was no diversion of funds as alleged by the authorities and it granted the relief to the assessee on all three counts.
- On appeal:

### Held

Even assuming that it was part of an integrated steel plant and because of various factors they could not manufacture the electricity and supply the same, there was no justification for 'P' to lend a sum to 'S' as unsecured loans. Assuming that the transaction also to be treated as *bona fide* transaction, absolutely there is no justification for 'S' to invest the said amount in

purchasing the shares of the assessee. It is because of this inter-connection between these two concerns, in which there are common directors, that the Assessing Authority and the Appellate Authority rightly held that it is a sham transaction, not a *bona fide* one and, therefore, they disallowed the interest on borrowed funds. Unfortunately, the Tribunal did not look into all three transactions as one transaction. It was of the view because 'P' did not take off and because of the memorandum of understanding entered into between the parties towards the purchase of the electricity, which is not in dispute, it was of the view that the transaction cannot be held to be a sham transaction. However, it holds that the amount invested by 'P', is money, which the assessee had raised from the shareholders, it is not a part of borrowed amount. Absolutely, there is no material to substantiate this particular aspect, thereby the Tribunal also accepts if this represents the borrowed money that transaction cannot be sustained. [Para 12]

Both the authorities below on a careful scrutiny of the material on record and on the basis of the admission of the Managing Director, which is found in the affidavit, have recorded the aforesaid findings. It is based on the legal evidence. Such concurrent findings of fact had been disturbed by the Tribunal without there being any evidence to the contrary. That is not the scope of appeal, in which the Appellate Authority could have interfered with the concurrent findings of fact. In that view of the matter, the said finding is also unsustainable. Accordingly, it is hereby set aside. [Para 13]