

No increase in ALV of property if interest-free loan was taken prior to tenancy

Summary – The Kolkata ITAT in a recent case of Gentex Merchants (P.) Ltd., (the Assessee) held that where receipt of interest free loan by assessee from holding company had occurred prior to grant of tenancy by assessee to principal shareholder of holding company (tenant), it could not be held that interest free loan was in nature of interest free deposit from tenant

Facts

- The assessee was the owner of a palatial bungalow in New Delhi. The property was let out to one LN on a monthly rent of Rs. 5 lakhs under an agreement dated 8-9-2006.
- MI was the holding company of the assessee. The holding company had taken a long term foreign currency loan which the assessee had received from the holding company. LN was the principal shareholder of the holding company (lender) MI.
- The Assessing Officer was of the view that the monthly rent of Rs.5 lakhs received by the assessee for letting out such a palatial property was very low. He was of the view that the very reason for charging such a small amount of rent was the interest free loan which had been received from MI by the assessee and that the interest chargeable on the loan by the holding company had been compensated by subsidised rent. He was of the view that the whole purpose was to compensate the low rent charged by the assessee from LN.
- On appeal, the Commissioner (Appeals) however held that the interest free loan was given prior to the tenancy between the assessee and LN and the amount in question was received by the assessee from the holding company and not from the tenant LN. He therefore held that the very basis on which the Assessing Officer concluded that the interest free loan was in the nature of interest free deposit from the tenant was factually unfounded.
- On appeal to the Tribunal:

Held

- The loan which the assessee received had no connection with the tenancy of LN. The amount in question was received by the assessee from the holding company and not from the tenant. Interest free loan was received during the period when construction of the property was in progress. The loans were received from the holding company in order to meet the cost of construction and cost of acquisition of the property. Therefore the receipt of interest free loan from the holding company was an event which had occurred prior to grant of tenancy and as such these two events apparently did not have any connection. The Commissioner (Appeals) therefore was right in holding that the very basis on which the Assessing Officer concluded that the interest free loan was in the nature of interest free deposit from the tenant was factually unfounded. The arrangement between the parties was therefore real and not sham. In such circumstances it is not possible to ignore the

agreements and conclude that the agreements have to be disregarded as it results in lesser tax burden on an assessee.

Thus, the claim of the revenue for ignoring the agreements between the parties is not sustainable.