

ITAT upheld disallowance of interest exp. as assessee had no interest free funds to give interest free loan

Summary – The Ahmedabad ITAT in a recent case of Bombay Sales Corporation., (the Assessee) held that where assessee claimed deduction of interest paid on borrowed capital and it had given interest free loan to a relative, since no interest free own funds were available at disposal of assessee, disallowance of proportionate interest expenses was justified

Facts

- The assessee, a partnership firm, claimed deduction of interest paid on borrowed capital.
- The Assessing Officer found that the assessee had given interest free loans and advances to two parties, namely, 'K' and 'S', which were connected to the partners of the firm. He observed that the assessee had not discharged the onus to prove that the claim towards interest expenditure incurred was for business purposes in terms of section 36(1)(iii). The assessee did not furnish any fund flow statement to show that there was no diversion of interest bearing funds towards aforesaid interest free advances. He accordingly disallowed proportionate interest incurred for non business purposes.
- The Commissioner (Appeals) upheld the order of the Assessing Officer.
- On second appeal:

Held

- The assessee has agitated the disallowance of proportionate interest expenses on certain advances made to parties which are connected to the partners of the assessee-firm. It is noticed that the assessee had given advance to 'K'. The outstanding amount at the beginning of the year to her was Rs. 2.32 lakhs, which swelled to Rs. 8.17 lakhs at the end of the year. Similarly another advance was given to 'S'. Advance at the beginning of the year to her was Rs. 15.57 lakhs, which grew to Rs. 27.08 lakhs at the end of the year.
- The assessee has paid interest on the capitals of the respective partners. Thus no interest free own funds are available at the disposal of the assessee-firm. Clearly assessee-firm on the one hand incurred the expenditure towards interest on the capital outstanding for the respective partners, whereas interest free advances have been made to the relatives of the partners. No business justification has been brought on record at any state before the revenue authorities for doing so. No justification has been brought before the Tribunal either. It is the repeated contention of the assessee that the advances have been funded out of profits available during the year. But for general assertion, nothing has been brought on record to show that profits so generated have been employed towards advances. Nearly Rs. 18 lakhs in aggregate was outstanding at the beginning of the year against which the interest has been paid to the partners on their corresponding capitals. The payments made during the year are out of mortgage account which gives an impression that the

assessee has been paying interest while advancing interest free loans. The lower authorities have rejected various contentions of the assessee on the ground that no fund flow statement has been furnished before them to appreciate assessee's perspective. Any such statement or other evidences have also not been furnished before the Tribunal which could establish usage of non interest bearing funds. Needless to say, onus lies on assessee to establish that expenditure has been incurred for business purposes to enable it to claim deduction under section 36(1)(iii).

- The assessee has relied upon the order of the Coordinate Bench of the Tribunal in its own case in IT Appeal No. 2433 (Ahd.) of 2013 relevant to assessment year 2010-11 to seek to set aside the issue to the file of the Commissioner (Appeals). It is admitted position that the partners' capital during the year in appeal is not interest free funds at the disposal of the partnership firm. The profit belongs to partner and gets added to the capital on which interest is payable by the firm. On these facts, one does not see any purpose of sending the issue back to the file of Commissioner (Appeals). The assessee has not been able to justify as to what facts required to be re-examined by the revenue. It is the assessee which has failed to discharge the onus in spite of specific opportunities in this regard. The assessee has not been able to make out any demonstrable case to show the availability of interest free funds at its disposal to support its claim for remitting the matter back to the file of the Commissioner (Appeals).
- Therefore, the appeal of the assessee was liable to be dismissed.