

IN THE INCOME TAX APPELLATE TRIBUNAL
COCHIN BENCH, COCHIN
BEFORE S/SHRI CHANDRA POOJARI, AM & GEORGE GEORGE K., JM

ITA No.749 /Coch/2019
Assessment Year: 2004-05

The Assistant Commissioner of Income-tax,Circle-1, Kollam	Vs.	M/s. Abdul Rehman Kunju, Cashew Exporters, Chandanathope, Kollam-691 014. [PAN: AABFM 3192J] ,
(Revenue -Appellant)		(Assessee Respondent)

ITA No. 62/Coch/2020
Assessment Year: 2007-08

M/s. Abdul Rehman Kunju, Cashew Exporters, Chandanathope, Kollam-691 014. [PAN: AABFM 3192J]	Vs.	The Assistant Commissioner of Income-tax,Circle-1, Kollam
(Assessee -Appellant)		(Revenue-Respondent)

Assessee by	Shri Iype Mathew, CA
Revenue by	Shri Mritunjaya Sharma, Sr. DR

Date of hearing	11/03/2020
Date of pronouncement	13/03/2020

ORDER

Per CHANDRA POOJARI, AM:

These two appeals filed by the Revenue and the assessee are directed against different orders of the CIT(A), Trivandrum and pertain to the assessment years 2004-05 and 2007-08.

2. First we shall take up the Revenue's appeal in ITA No.749/Coch/2019 for the assessment year 2004-05. The Ld. AR has submitted that the tax effect in this case is below the limit prescribed in CBDT Circular 17/2019 dated 08/08/2019 for filing an appeal before the ITAT.

3. It is observed that as per the latest Circular of CBDT, the Assessing Officer is required to file an appeal before ITAT only if the tax effect is more than 50 lakhs. Thus, taking note of CBDT Circular No. 17/2019 dated 08/08/2019 and considering the fact that the tax effect in the instant appeal is less than Rs. 50 lakhs, the present appeal deserves to be dismissed as not maintainable. However, we make it clear that the issue(s) raised in the instant appeal is left open to be examined in the appropriate proceedings, if arises, in future. At the same time, we also make it clear that if the appeal falls in any of the exceptions referred to in the above said CBDT Circular, the Revenue is at liberty to move an application for recalling the order, if

so, advised. Accordingly in the light of CBDT Circular No. 17/2019 dated 08/08/2019, the appeal filed by the Revenue stands dismissed.

3. Next, we shall take up the assessee's appeal in ITA No. 62/Coch/2020 for the assessment year 2007-08. The assessee has raised the following grounds of appeal:

1. The Order of the Commissioner of Income Tax(Appeals),Trivandrum is against law, facts and circumstances of the case.
2. The CIT(Appeals) has erred in following the decision of the Kerala High Court in the case of V.I. Baby (123 Taxman 894) and sustained the disallowance of Rs 94,592/- being the proportionate bank interest and drawings of Rs. 46,77,466/- made by the Managing Partner of the firm, whose Capital and Current Account balance as on 01.04.2006 was Rs 8,78,50,660.40 and his share of profit for the year was Rs. 15,89,498.67 and even after the above withdrawal the capital and current account balance was Rs 8,47,62,693.07.
3. The CIT(A) should have noted that in the case of V.I. Baby, there was only debit balance in the capital account of the partners and therefore the facts of that case was different from that of the Appellant's case.
4. The CIT(Appeals) has erred in not following the Supreme Court decision in Hero Cycles Ltd Vs. CIT (379 ITR 347), the ratio of which was squarely applicable to the Appellant's case.
5. The CIT(Appeals) should also have noted that the Supreme Court has already held in the case of Munjal Sales Corporation Vs. CIT , 298 ITR 298, that interest on diversion of funds was not disallowable, if sufficient own funds were available with the assessee.
6. The CIT(A) also erred in not following the decision of the Jurisdictional Tribunal decision in DCIT Vs. S. Jameela , ITA No. 704/ Coch/ 2010 dtd 20/07/2010.

4. The facts of the case are that the assessee had paid bank interest of Rs.3,33,896 and the same was debited in the profit and loss account. The balance in the Federal Bank PCFC loan was Rs.1,29,49,690/- as on 31.03.2007. Verification of the current account of partner Abdul Rehman Kunju showed that Shri Abdul Rehman Kunju had effected drawings of Rs.46,77,466/-. The details regarding the drawings were called for from the assessee. As per the details filed, out of the drawings, an amount of Rs.36,68,000/- had been gifted by the assessee to Shri Hamsa Ramla and Sirajudeen. The Assessing Officer proposed to disallow a portion of bank interest on the ground that interest bearing funds had been diverted for non business purposes. The Assessing Officer observed that the purpose of making the gift was not explained by the assessee and the assessee has also not proved that the gift was made by the assessee out of commercial expediency. The Assessing Officer relied on the judgment of the Delhi High Court in the case of New India Colour Co. vs. CIT (80 ITR 206) wherein it was held that gift by partner out of his capital account is not valid amount and interest paid on such gifted amount is not allowable. The Assessing Officer also relied on the judgment of the Kerala High Court in the case of V.I. Baby & Co. (254 ITR 248) wherein it was held that so long as the assessee was not the beneficiary on the investment made and so long as the advances were interest free, disallowance of interest in proportion to the advance made is justified. In the circumstances, the Assessing Officer disallowed the amount of Rs.94,592/- out of the interest payment attributable to interest paid on funds diverted for non business purposes viz. gifts made.

5. On appeal, the CIT(A) rejected the argument of the assessee that interest free funds were available for advancing the interest free loans to sister concerns. The CIT(A) sustained the addition of Rs.94,592/- made by the Assessing Officer by following the decision of the Jurisdictional High Court in the case of V.I. Baby (123 Taxman 894).

6. Against this, the assessee is in appeal before us. The Ld. AR submitted that the Shri M. Abdul Rehman Kunju, Managing Partner of the assessee firm had drawn Rs.46,77,466/- from the business during the relevant assessment year. According to the Ld. AR, the bank interest paid for a short period on a packing credit advance of Rs.1,29,49,690/- was Rs.3,33,896/-. The Ld. AR submitted that the capital and current account balance of this partner in the firm as on 01/04/2006 was Rs.8,78,50,660.40, his share of profit for this year was Rs.15,89,498.67. The Ld. AR submitted that even after the withdrawal of Rs.46,77,466/-, the credit balance in the capital and current account of the assessee was Rs.8,47,62,693.07. The Ld. AR relied on the judgment of the Supreme Court in the case of Hero cycles Pvt. Ltd. vs. CIT 379 ITR 347 wherein it was held that when the assessee had sufficient own capital, he can utilize that fund for non business purposes and no disallowance can be made for diversion of funds. The Ld. AR also relied on the decision of the co-ordinate Bench of this Tribunal in the case of DCIT vs. S. Jameela in ITA No. 704/Coch/2010 dated 20/07/2010 wherein it was held that if there is sufficient capital balance even after the withdrawal no diversion of the interest bearing funds

can be alleged. In view of the above decisions, the Ld. AR submitted that the disallowance of Rs.94,592/- was not legally tenable.

7. The Ld. DR relied on the orders of the lower authorities.

8. We have heard the rival submissions and perused the material on record. A similar issue came up for consideration before this Tribunal in the case of S. Jameela vs. ACIT in ITA No. 704/Coch/2010 dated 20/07/2012 wherein it was held as follows:

“6. We have heard the rival contentions on this issue. With regard to the investment made in the South Indian Bank by way of deposits and purchase of its shares, the Ld. CIT(A) has observed as under:

*“13. As regards investment in South Indian Bank, which is the banker of the appellant, in the form of FDs and shares, the assessee’s explanation seems to be reasonable, **since these investments and deposits have been made to keep and maintain high priority relation with the bankers to gain business benefits** and as the appellant has explained that these were basically to obtain for Letters of Credit to be opened for the import of raw cashew nuts, which is the business of the appellant”.*

With regard to the above deposits made with the Bank and purchase of its shares, in our view, the question of diversion of funds does not arise at all, as the assessee has stated the purpose of making the deposits and purchasing the shares. It is further to be noticed that these deposits have been made by the assessee in her name/concern’s name and the said deposits have been disclosed in the assessee’s books of accounts. In the instant case, there may be many reasons for the assessee to park funds in the form of deposits with the Bank, from whom she has obtained loans. It is a known fact that a prudent businessman will not normally make deposits in the Bank which usually fetches lower interest, by using the loan funds on which he is liable to pay interest at a higher rate, unless there is some business compulsion for doing so. It is also well established principle that the tax authorities cannot sit

on the chair of the businessman and dictate the manner of carrying on the business. Further, in our view, the question of diversion of funds shall arise only if money was taken away from the concern of the assessee and was given to another concern for non-business purposes without charging interest at reasonable rates. This is not so in the instant case. Hence, we do not find any infirmity in the decision of the Ld. CIT(A) in holding that the funds deposited in the South Indian Bank in the form of deposits and shares are for business purposes.

7. *With regard to the gift of Rs. 58.50 lakhs given to the husband of the assessee, we are of the view that the said payment should be considered as a withdrawal made by the assessee from her capital for personal purpose. The Assessing Officer has noted in para 3.6(b) of the assessment order that the capital of the assessee stood at Rs. 3.59 crores as on 01-04-2006 and Rs. 3.08 crores as on 31-03-2007. Even if the gift of Rs. 58.50 lakhs referred above is deducted from the capital account, it is seen that the assessee is still possessing sufficient capital. Accordingly, we are of the view that that the gift amount of Rs.58.50 lakhs should be treated as a personal withdrawal and hence it cannot be considered as diversion of funds, since the assessee is in possession of sufficient capital. Accordingly, we set aside the order of the Ld. CIT(A) on this issue and direct the Assessing Officer not to treat the same as diversion of funds.*

8.1 In this case of Shri Abdul Rehman Kunju, the current account with the firm is as follows:

Shri Abdul Rehman Kunju

Date 01-04-2004	Opening balance 84,76,410.71	Drawings for the year 46,77,466.00
31-03-2005	Profit for the year 15,89,498.67	31-03-2015 Cl./B/L 53,88,443.38
Total	<u>Rs.1,00,65,909.38</u>	<u>Rs.1,00,65,909.38</u>

Thus, the partner has withdrawn his own funds from his current account with the firm. It cannot be said that the assessee's funds should be used for business purposes only and the partners' cannot withdraw their money which leads to the firm borrowing interest bearing funds. In our opinion, this issue is squarely covered by the decision of this Tribunal in the case of S. Jameela vs. ACIT in ITA No. 704/Coch/2010 dated 20/07/2012.

8.2 Further, we have gone through the reconstituted partnership deed dated 31st March, 1994 and 28th June, 2018. As per the latest reconstituted partnership deed dated 28th June 2018, clause 6 specifically mentions that the partners are at liberty to withdraw any amount from the partnership against the amount outstanding in his credit in the firm. Being so, withdrawal of money by the partner from his current account does not carry any interest and he is at liberty to draw the same from his current account. Accordingly, we find force in the argument of the Ld. AR that no

proportionate disallowance of interest could be made. Hence, we allow the ground taken by the assessee. Thus, the appeal of the assessee in ITA No.62/Coch/2020 for the assessment year 2007-08 is allowed.

9. In the result, the appeal of the Revenue is dismissed and the appeal of the assessee is allowed.

Order pronounced in the open court on 13th March, 2020.

sd/-
(GEORGE GEORGE K.)
JUDICIAL MEMBER

sd/-
(CHANDRA POOJARI)
ACCOUNTANT MEMBER

Place: Kochi

Dated: 13th March, 2020

GJ

Copy to:

1. M/s. Abdul Rehman Kunju, Cashew Exporters, Chandanathope, Kollam-691 014.
2. The Assistant Commissioner of Income-tax, Circle-1, Kollam.
3. The Commissioner of Income-tax(Appeals), Trivandrum
The Pr. Commissioner of Income-tax, Trivandrum.
4. D.R., I.T.A.T., Cochin Bench, Cochin.
5. Guard File.

By Order

(ASSISTANT REGISTRAR)
I.T.A.T., Cochin

I.T.A. Nos.749/ Coch/2019 and
62/Coch/2020