
(2005) 04 AHC CK 0235
In the Allahabad High Court
Case No : Income Tax R. No. 89 of 1996

Commissioner of Income Tax	Vs	APPELLANT
Prem Heavy Engineering Works P. Ltd.		RESPONDENT

Date of Decision : 25-04-2005

Acts Referred:

Income Tax Act, 1961 — Section 256(2)

Citation : (2006) 285 ITR 554 : (2006) 150 TAXMAN 90

Hon'ble Judges : Rajes Kumar, J; R.K. Agrawal, J

Bench : Division Bench

Final Decision : Dismissed

Judgement

1. The Income Tax Appellate Tribunal, New Delhi, has referred the following question of law u/s 256(2) of the Income Tax Act, 1961 (hereinafter referred to as "the Act") for opinion to this court:

Whether, on the facts and in the circumstances of the case, the hon"ble Income Tax Appellate Tribunal was justified in confirming the deletion of Rs. 1,81,000 being disallowance of interest ?

2. The present reference relates to the assessment year 1984-85.

3. Briefly stated the facts giving rise to the present reference are as follows:

4. The respondent-assessee has been assessed to Income Tax in the status of a company. During the assessment year under consideration, it had advanced a sum of Rs. 37,47,583 to its sister concern, namely, M/s. Prem Engineering Works P. Ltd. on various dates. Whereas the services provided by the said sister concern for job work came to the extent of Rs. 21,58,191. The respondent-assessee had also an opening debit balance of Rs. 30,34,337 in the name of the sister concern. The Assessing Officer was of the view that the respondent-assessee having paid interest on overdraft facilities, it should not make any interest-free advances to its sister concern and, accordingly, disallowed a sum of Rs. 1,81,000 from the

interest paid on overdraft. Feeling aggrieved, the respondent-assessee preferred an appeal before the Commissioner of Income Tax (Appeals) who has allowed the appeal and deleted the addition on the following grounds:

I have heard learned Counsel and gone through the facts of the case. From the perusal of the facts brought on record I find that during the year under consideration, the appellant has got interest-free advances from its customers to the extent of Rs. 1 crore. In addition to these interest-free advances, the appellant has reserve and share of capital to the tune of Rs. 60.45 lakhs. The interest-free advances at Rs. 37 lakhs and odds to the sister concern are fully covered by the interest-free advances reserve and capital of the appellant. Therefore, it cannot be said that the appellant has diverted any fund on which it has paid interest to its sister concern on which no interest was charged. This practice has been adopted by the appellant even in the preceding year where it has been accepted. Even in the succeeding year such plea of the appellant has been accepted. There is no dispute over the fact that the appellant has taken the overdraft facilities for the purpose of business. The position being so, no part of the interest can be disallowed in view of the decision of the Madras High Court in the case of Commissioner of Income Tax, Madras Vs. Pudukottai Company P. Ltd., . A similar view has been taken by the Madhya Pradesh High Court in the case of D and H Secheron Electrodes Pvt. Ltd. Vs. Commissioner of Income Tax, , where the facts of the case were that the Income Tax Officer disallowed part of the interest paid by the assessee on the capital borrowed by it for the purpose of its business on the ground that the assessee has given advances to some concerns without charging interest and this was upheld by the Commissioner of Income Tax (Appeals) and the Tribunal. On reference, the hon'ble Madhya Pradesh High Court held that the disallowance of part of the interest was not justified. It is interesting to note that the appellant has given similar interest-free advances to similar other parties who are doing the same job work/supply of machinery or the appellant but no adverse view has been taken by the Assessing Officer in respect of those parties. Considering the facts of the case and legal position, I would delete the addition of Rs. 1,81,000.

5. The Revenue's appeal before the Tribunal has failed.

6. We have heard the learned Counsel for the parties.

7. Learned standing counsel submitted that as the respondent-assessee had borrowed money from the bank and had paid interest over the same to the banker and any amount which is interest-free loan given to the sister concern, payment of corresponding amount of interest on overdraft on pro rata basis has rightly been disallowed. The submission is misconceived. From the reply submitted by the respondent-assessee to the query made by the Assessing Officer as to why the amount be not disallowed, the respondent-assessee had submitted as follows:

The assessee-company had got its own funds and interest-free advances as

follows:

Rs. (a) own funds, share capital 9,70,000 surplus and reserves (Rs. 50,75,000) 50,75,000 60,45,000 b) Interest-free advances: M/s. Godawari Sugar Mills 17,80,000 Polymech Sugar Mills 82,20,000 1,00,00,000 The above interest-free advances were at the close of the relevant accounting year. In the beginning of the said year, the interest-free advances were as follows:

Rs. M/s. Polymech Sugar Mills 33,00,000 M/s. Godawari Sugar Mills 17,00,000 50,00,000

If at all it is to be considered that the assessee has interest-free advances to its sister concern, reasonable presumption that when the assessee has its own capital and interest-free advances, the same could have been utilized in the said non-business advances. It cannot, therefore, be presumed that the assessee has made interest-free advances out of funds borrowed from the bank on which interest has been paid. The overdraft from the bank has been clearly taken for working the capital which has been totally used for the assessee's business."

8. From the perusal of the reply reproduced above, we find that the respondent-assessee had sufficient amount of money towards share capital, surplus and reserve as also interest-free advances by the two companies which was about Rs. 1,60,00,000. Thus, the interest-free advances made to the sister concern, namely, M/s. Prem Engineering Works was fully covered from the interest-free advances which was share capital, surplus and reserve with the respondent-assessee had. This court in the case of Commissioner of Income Tax Vs. Radico Khaitan Ltd., had considered this aspect and has held that where the amount of any interest-free loan is sufficiently covered by the non-interest-bearing funds available with the assessee, the question of disallowance of interest on borrowed funds does not arise. It is also not the case of the Revenue that any amount borrowed from the bank on which the liability for payment of interest-free advance was there with the respondent-assessee, had not utilized for the purposes of business.

9. Respectfully following the aforesaid decision, we answer the question referred to us in the affirmative i.e. in favour of the assessee and against the Revenue. However, there shall be no order as to costs.