

Interest disallowed as sum advanced by builder for acquisition of property wasn't utilized by AE for said purpose

Summary – The High Court of Karnataka in a recent case of Embassy Development Corporation., (the Assessee) held that where assessee-builder advanced borrowed amount to its sister concern for purpose of acquiring a portion of property in project proposed to be developed by its sister concern and said amount was not utilised for said project but it was used for some other project, assessee was not entitled for deduction of interest paid on borrowed amount

Facts

- The assessee-firm was engaged in the business of real estate and construction of commercial and residential complexes.
- The assessee borrowed a sum of Rs. 2.50 crores from KSIIDC as medium term corporate loan for its business. However, the said amount was diverted to its sister concern for which, one of the partners of the assessee-firm was also one of the directors. The assessee debited a sum of Rs. 30.49 lakhs as interest towards loan amount and claimed it as an expenditure while preparing the profit and loss account and filed the returns.
- The Assessing Officer disallowed the assessee's claim of interest paid on the ground that though the assessee availed loan from KSIIDC, the same was diverted to its sister concern, the amount received was not utilized for the business of the assessee and no income had accrued to the assessee.
- On appeal, the First Appellate Authority denied the expenditure on interest.
- On second appeal, the Tribunal held that though the assessee availed loan for its business, the said amount was not utilized for its business whereas the same was diverted to its sister concern. The veracity of exchange of letter between the assessee and its sister concern to treat the loan as an advance payment for the area to be purchased in the project, was not above board. The said sister concern had not yet started the project. Hence, the assessee was not entitled for any deduction towards interest paid on the loan availed and dismissed the appeals.
- On appeal:

Held

- The authorities below clearly held that the transaction between the assessee and its sister concern is purely a loan transaction. There is no agreement entered into between the parties. The intention behind the advance is only to book interest expenditure in the assessee's case to reduce the taxable income. The finding recorded by the authorities below is purely a question of fact. The same was confirmed by the Tribunal. Except saying that the sister concern provisionally agreed to allot an extent of 30000 sq.ft. and 25 covered car park area in the project, no concrete material has been produced before the authorities concerned. Initially, the assessee itself wanted to put up said

projects, however, the responsibility of construction has been given to its sister concern. The land belongs to another sister concern. Even after three years, the project has not yet been commenced.. In view of that, all the authorities have concurrently held that the amount advanced is not a business expediency and it is only a loan transaction. Hence, the assessee is not entitled for any deduction towards the interest paid for availing the loan. There is no infirmity or irregularity in the said finding.