

**THE INCOME TAX APPELLATE TRIBUNAL,
'SMC' BENCH, KOLKATA**

**Before Shri Rajpal Yadav, Vice-President (KZ)
&
Shri Girish Agrawal, Accountant Member**

**I.T.A. No. 144/KOL/2024
Assessment Year: 2020-2021**

***Bal Krishan Das Mundhra,.....Appellant
66, Purnadas Road,
Kolkata-700029
[PAN:AIKPM4239P]***

-Vs.-

***Income Tax Officer,.....Respondent
Ward-12(1), Kolkata,
Assessment Unit,
Income Tax Department,
Aayakar Bhawan,
P-7, Chowringhee Square,
Kolkata-700069***

Appearances by:

Sm. Mita Rizvi, CA, appeared on behalf of the assessee

*Smt. Ranu Biswas, Addl. CIT, D.R., appeared on behalf
of the Revenue*

Date of concluding the hearing : April 08, 2024

Date of pronouncing the order : April 09, 2024

O R D E R

Per Rajpal Yadav, Vice-President (KZ):-

The assessee is in appeal before the Tribunal against the order of ld. Commissioner of Income Tax (Appeals), National

Faceless Appeal Centre (NFAC), Delhi dated 07.12.2023 passed for A.Y. 2020-21.

2. The assessee has taken five grounds of appeal, out of which Grounds No. 4 & 5 are general grounds, which do not call for recording of any specific finding.

3. In Grounds No. 1 to 3, only one common issue is involved, namely whether Revenue Authorities are justified in disallowing the deduction of Rs.34,23,294/- under section 57 of the Income Tax Act on the ground that assessee has not made the payment of interest expenses.

4. Brief facts of the case are that the assessee has filed its return of income on 30.12.2020 declaring total income of Rs.2,81,829/-. The case of the assessee was selected for scrutiny assessment and a notice under section 143(2) was issued and served upon the assessee.

5. On perusal of the accounts, it revealed to the ld. Assessing Officer that the assessee has shown interest income of Rs.1,32,22,133/- from Simplex Projects Limited. He also claimed interest expenditure of Rs.1,29,23,294/- as paid to Bikaner Land & Properties LLP. The ld. Assessing Officer further found that this interest expenditure has been claimed under section 57 of the Income Tax Act. He observed that on examination of Ledger Account of Bikaner Land & Properties LLP, it revealed that the assessee has actually paid interest of Rs.95,00,000/- only.

Therefore, he sought explanation of the assessee as to why the difference between the interest expenditure claimed by the assessee in the accounts, vis-à-vis actually paid should not be added back to the total income of the assessee. The assessee filed a detailed submission. However, Id. Assessing Officer was not satisfied with the submission of the assessee. He disallowed the interest expenditure of Rs.34,23,294/- and made the addition to the total income of the assessee. In this way, total income has been determined at Rs.37,05,123/-.

6. Appeal to the Id. CIT(Appeals) did not bring any relief to the assessee.

7. Ld. Counsel for the assessee while impugning the orders of Revenue Authorities has filed a detailed written submission and her submission reads as under:-

SUBMISSION OF THE APPELLANT:

Ground Nos.1 -3: Disallowance of deduction of Rs.34,23,294/- claimed u/s.57 of the Act on account of interest payment due for the relevant financial year without appreciating the fact that the same was paid subsequently before filing the return of income for the relevant assessment year and the assessee is maintaining his books following mercantile system of accounting

The brief facts of the case are that the assessee maintains his accounts following mercantile system of accounting.

Following the mercantile system of accounting, the assessee accounted for the interest receipt of Rs.1,32,22,133/- in his Profit & Loss A/c for the relevant financial year (*enclosed at page 38 of the P/b*), although the same remain accrued till the end of the relevant financial year. Attention is invited here to the **ledger account of Simplex Projects Ltd. for the FY 2019-20** as appearing in the books of the assessee, *enclosed at pages 53-54 of the P/b*.

From a perusal of the same, it can be seen that the entire interest income as shown receivable from M/s.Simplex Projects Ltd., which was accounted for in the books and was offered for taxation during the relevant assessment year, remain accrued till the end of the relevant financial year and was not received during the relevant assessment year.

Again, following the mercantile system of accounting, the assessee accounted for interest payment of Rs.1,29,23,294/- for the relevant financial year and claimed deduction of the same u/s.57 of the Act, even though a total sum of Rs.95,00,000/- only was actually paid during the relevant financial year to the lender, M/s.Bikaner Land & Properties LLP. In this regard, reference is invited to the **letter as given by the lender, M/s.Bikaner Land & Properties LLP** acknowledging receipt of interest to the tune of Rs.95,00,000/- for the FY 2019-20 as against total interest due of Rs.1,29,23,294/-, as enclosed at page 47 of the P/b.

The balance interest due of Rs.34,23,294/- was paid to the lender in the subsequent financial year on 14/09/2020 vide cheque drawn from UCO Bank for Rs.70,00,000/-. Reference is invited here to the **intimation letter as given by the assessee to the Accounts Department of Bikaner Lands & Properties LLP** intimating payment of Rs.70,00,000/- on 14/09/2020, enclosed at page 50 of the P/b.

From a perusal of the above, it may be seen that it is clearly mentioned in the said intimation letter that the total sum of Rs.70,00,000/- paid on 14/09/2020 includes the interest payment due of Rs.34,23,294/- relating to FY 2019-20.

In this connection, further reference is invited to the **confirmation as given by Bikaner Lands & Properties LLP acknowledging receipt of outstanding interest of Rs.34,23,294/- relating to FY 2019-20** which was included in the sum of Rs.70,00,000/- paid by the assessee on 14/09/2020, enclosed at page 65 of the P/b.

Now, in this context, it would be of relevance to throw light on the provisions of **sec.145** of Income Tax Act, 1961, reproduced as under:

"Method of accounting.

145. (1) Income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" shall, subject to the provisions of sub-section (2), be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee.

(2) The Central Government may notify in the Official Gazette from time to time income computation and disclosure standards to be followed by any class of assesseees or in respect of any class of income.

(3) Where the Assessing Officer is not satisfied about the correctness or completeness of the accounts of the assessee, or where the method of accounting provided in sub-section (1) has not been regularly followed by the assessee, or income has not been computed in accordance with the standards notified under sub-section (2), the Assessing Officer may make an assessment in the manner provided in section 144."

As seen from the above, sec.145 of the Act lays down the rules for accounting methods that assesseees should follow when calculating their taxable income. The said section allows assesseees to use either the cash basis or accrual basis of accounting.

Under cash basis of accounting, the time of recording a transaction in books of accounts is when there is inflow or outflow of cash, while, under mercantile system of recording, a transaction is recorded when an income or an expense accrues. In this method, the transactions are recorded despite whether the cash is received or paid.

It thus undoubtedly follows from the above that the assessee following the mercantile system of accounting, accounted for both interest income and interest payment for the relevant financial year on accrual basis, which is perfectly within the four corners of law.

Reliance here is placed on the decision of the Hon'ble **Supreme Court** in the case of **Kerala State Industrial Development Corpn. Ltd. v. Commissioner of Income-tax** reported in **128 Taxman 29 (SC)**, wherein relying on sec.145 of the Act it was held that since the assessee had followed cash system of accounting in respect of interest income, the computation of chargeable interest is to be allowed on the basis of the amount of interest actually received.

Relevant extract of the judgment reproduced as under:

"In arriving at the conclusion, the High Court had overlooked the opening words of section 5 which make the provisions of the said section 'subject to the provisions of the Act.' The other provisions of the Act include section 21 whereunder provisions of certain specified sections and schedules of the Income-tax Act have been made applicable with necessary modifications as if the said provisions referred to the Interest-tax Act instead of the Income-tax Act. At the material time section 145 of the Income-tax Act was incorporated in the Interest-tax Act by virtue of section 21 of that Act. Section 145 of the Income-tax Act permits income chargeable under the head 'Profits and gains of business or profession' or 'Income from other sources' to be computed in accordance with either the cash or mercantile system of accounting, as may be regularly employed by the assessee. The assessee had followed the cash system of accounting in respect of the interest income. Therefore, section 5 of the Interest-tax Act would in the circumstances allow the calculation or computation of chargeable interest on the basis of the amount of interest actually received."

As such, taking into consideration the above, the following conclusion can be drawn in the present case of the assessee that following the mercantile system of accounting the assessee has correctly accounted for the interest income of Rs.1,32,22,133/- during the relevant financial year and has offered the same for taxation in the computation of total income for the relevant assessment year, even though the same was not actually received during the relevant financial year. Again, the total interest expense of Rs.1,29,23,294/- [which included interest due and not paid during the relevant financial year of Rs.34,23,294/-] was correctly accounted for and claimed as deduction u/s.57 of the Act in the computation of total income for the relevant assessment year following the same mercantile system of accounting. Therefore, the addition made by the Ld.AO disallowing the claim of balance interest payable of Rs.34,23,294/- for the relevant financial year is totally illogical, especially more so, when already the Ld.AO has accepted the accounting of interest income on accrual basis. Undoubtedly, the AO has acted arbitrarily in accepting the accounting of interest income on accrual basis while rejecting the accounting of interest expense on accrual basis.

The above action of the AO is totally incorrect as he cannot simply accept accrual basis of accounting for interest income and cash basis of accounting for interest expense.

The above proposition has been upheld by the **Apex Court** in the case of **Indore Malwa United Mills Ltd. v. State of Madhya Pradesh** reported in **060 ITR 0041**, in which case it was held as under:

"Held, that, as the appellant produced before the assessing authorities all its registers, it was their duty to definitely come to one conclusion or the other in regard to the reliability of every one of the relevant accounts filed by the appellant, and in the absence of any

such finding it was not open to them to pick and choose some of the registers, which were more favourable to the revenue.”

Further, as regards the allegation of the Ld.CIT(A) that the certificate as given by the lender, M/s.Bikaner Land & Properties LLP on 03/03/2022 (enclosed at page 47 of the P/b) did not acknowledge the receipt of balance interest due of Rs.34,23,294/- relating to FY 2019-20, claimed to be paid on 14/09/2020, it may be noted that in the said certificate the actual amount of interest received during the relevant FY 2019-20 [i.e. Rs.95,00,000/-] only was certified out of total interest expense of Rs.1,29,23,294/- for the relevant assessment year. Moreover, as far as the allegation that even M/s.Bikaner Land & Properties LLP never acknowledged the receipt of balance interest of Rs.34,23,294/- for the FY 2019-20, it needs mention that in the **confirmation as given by the said lender on 17/09/2020, enclosed at page 65 of the P/b**, above fact is clearly mentioned and acknowledged.

In view of the above, it is prayed most respectfully that the total claim of interest payment to the tune of Rs.1,29,23,294/- may be allowed and the disallowance made on account of interest due for the relevant financial year of Rs.34,23,294/-, claimed u/s.57 of the Act, maybe deleted.

8. Apart from this, ld. Counsel for the assessee took us through the finding of ld. CIT(Appeals) in paragraph no.14 of the impugned order, which reads as under:-

“14. The appellant has relied on various case laws citing the claim of interest on accrual basis. However, the issue here is whether the remaining interest, which has been claimed u/s 57, was actually paid in next financial year or not. It is inferred that this certificate was given on 03.03.2022 and the alleged balance interest was shown to be paid on 14.09.2020. So, even the under Bikaner Lander and Property LLP did not acknowledge the receipt of balance interest of Rs.34,23,294/- for the F.Y. 2019-20 in this certificate, which proves that Rs.34,23,294/-, which is alleged to be interest component included in the UCO Bank cheque dated 14.09.2020 for Rs.70,00,000/-, is principal amount of loan taken in subsequent year but not the interest for previous year loan. Further, when previous two installments of interest payments were exclusively interest payment only, why this remaining interest would be clubbed with principal amount and that too in shown paid to in next financial year. Thus, the appellant failed to discharge the onus of conclusively proving the balance interest payment with any cogent evidence. Hence, the disallowance made by the AO of excess claim of said interest payment of Rs.34,23,294/- as deduction u/s 57, is sustained. Ground of appeal No. 1 of the appellant is dismissed”.

9. She submitted that the ld. CIT(Appeals) has misread the certificate exhibiting the payment of Rs.70,00,000/- on 14.09.2020. She took us through the details of this payment and submitted that a sum of Rs.70,00,000/- do include Rs.34,23,294/-, which is the component of interest. In other words, the stand of the ld. Counsel for the assessee was that the assessee has been following mercantile system of accounting. It has recognized interest income of Rs.1,32,22,133/- on accrual basis. Actually, this total amount was not received by the assessee before the end of the accounting year. Similarly, the assessee has recognized the interest expenditure on accrual basis out of the total amount accrued to it. It has actually paid Rs.95,00,000/- and the balance was paid on 14th September in the next year. The ld. CIT(Appeals) has erred in creating artificial distinction to the sum of Rs.70,00,000/- paid in the next year. This sum contains the interest component also. Therefore, according to the ld. Counsel for the assessee, there cannot be a mixed system of accounting for assessment of income on accrual basis and disallowance of expenditure on cash basis.

10. The ld. D.R., on the other hand, submitted that if expenditure is not reflected in Form 26AS issued by the recipient, then, how it will be allowed to the assessee.

11. We have duly considered the rival contentions and gone through the record carefully. There is no dispute with regard to the fact that the assessee has been consistently following mercantile system of accounting. It has accounted its interest income on

mercantile system and not on receipt basis. This stand of the assessee was not disputed by the ld. Assessing Officer. We could appreciate the stand of the ld. Assessing Officer that if he excluded the interest income shown by the assessee to the extent, it was not received in this year by following cash system of accounting. Similarly, ld. Assessing Officer cannot disallow the expenditure worked out by the assessee on mercantile system of accountancy. The Hon'ble Supreme Court in the case of Kerala State Industrial Development Corporation Limited-vs. – CIT reported in 128 Taxman 29 (SC) relied upon by the ld. Counsel for the assessee has considered identical situation. Respectfully following the judgment of the Hon'ble Supreme Court relied upon by the ld. Counsel for the assessee, we allow this ground of appeal and delete the disallowance.

12. In the result, the appeal of the assessee is allowed.

Order pronounced in the open Court on 09/04/2024.

Sd/-

(Girish Agrawal)
Accountant Member

Kolkata, the 9th day of April, 2024

Sd/-

(Rajpal Yadav)
Vice-President (KZ)

*Copies to :(1) Bal Krishan Das Mundhra,
66, Purnadas Road,
Kolkata-700029*

*(2) Income Tax Officer,
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Assessment Unit,*

*Income Tax Department,
Aayakar Bhawan, P-7, Chowringhee Square,
Kolkata-700069;*

*(3) Commissioner of Income Tax (Appeals),
National Faceless Appeal Centre (NFAC), Delhi;*

(4) CIT- , Kolkata

(5) The Departmental Representative;

*(6) Guard File
TRUE COPY*

By order

*Assistant Registrar,
Income Tax Appellate Tribunal,
Kolkata Benches, Kolkata*

Laha/Sr. P.S.