

आयकर अपीलीय अधिकरण, जयपुर न्यायपीठ, जयपुर
IN THE INCOME TAX APPELLATE TRIBUNAL, JAIPUR BENCHES, JAIPUR

श्री भागचन्द, लेखा सदस्य एवं श्री कुल भारत, न्यायिक सदस्य के समक्ष
BEFORE: SHRI BHAGCHAND, AM AND SHRI KUL BHARAT, JM

आयकर अपील सं./ITA No. 453/JP/2016
निर्धारण वर्ष/Assessment Year : 2011-12

Assistant Commissioner of Income Tax Circle-02, Kota	बनाम Vs.	M/s Shiv Agrevo Ltd., Jahalawar Road, Kalmanda, Baran
स्थायी लेखा सं./जीआईआर सं./PAN No. AACCS7224F		
अपीलार्थी/ Appellant		प्रत्यर्थी/ Respondent

निर्धारिती की ओर से/ Assessee by : Shri Mahendra Gargieya
& Shri F.Rahman (Advocate)
राजस्व की ओर से/ Revenue by : Shri Ajay Malik (JCIT)

सुनवाई की तारीख/ Date of Hearing : 11/05/2017
घोषणा की तारीख/ Date of Pronouncement : 23/05/2017.

आदेश/ ORDER

PER: SHRI KUL BHARAT, J.M.

This appeal by the revenue is directed against the order of Id. CIT (A), Kota dated 12.02.2016 pertaining to assessment year 2011-12. The revenue has raised the following grounds of appeal:-

"On the facts and in the circumstances of the case, the Id. CIT(A)

has erred in:-

- "i. deleting trading addition of Rs. 27,86,979/- out of total addition of Rs. 32,86,979/-
- ii. deleting addition of Rs. 1,00,000/- out of total addition of Rs. 3,00,000/- made u/s 40A(2)(b) of the Act being excessive salary paid to one of the Directors;

- iii. deleting addition of Rs. 5,54,000/- made u/s 36(1)(iii) being diversion of higher interest bearing loan to sister concerns at lower rate of interest;
- iv. the appellant craves liberty to raise additional ground and to modify/amend the ground of appeal at the time of hearing."

2. Briefly stated facts of the case are that the assessee filed her return of income on 30.09.2011 declaring income of Rs. 5,54,64,250/-. The case was selected for scrutiny assessment and the assessment u/s 143(2) of the Income Tax Act, 1961 (hereinafter referred to as the 'Act') was framed vide order dated 25th March, 2014. While framing the assessment, the Assessing Officer rejected the books of account and applied Gross Profit rate @ 4.30%. Thereby, he made additions of Rs. 32,86,979/- apart from this the Assessing Officer made disallowance u/s 40A(2)(b) of the Act. In respect of salary paid to Shri Manish Sabo, a person specified u/s 40A(2)(b) of the Act of Rs. 3,00,000/- and also made disallowance of interest of Rs. 6,02,824/- on the basis that interest paid on account of advancing money to the sister concerns at lower rate and also made disallowance u/s 40A(2)(b) of the Act amounting to Rs. 5,54,000/- on basis that the amount was paid in cash in excess of the monetary limit. Hence the Assessing Officer made total addition of Rs. 4,68,17,23/- and assessed total income of the assessee at Rs. 6,01,59,367/- against the income declaring at Rs. 5,54,77,644/-.

3. Aggrieved by the order of the A.O., the assessee preferred an appeal before Id. CIT(A), who after considering the submissions, partly allowed the

appeal. The Id. CIT(A) had reduced the trading addition from Rs. 32,86,979/- to 5,00,000/- and also deleted the addition to extent of Rs. 2,00,000/- in respect of disallowance made u/s 40A(2)(b). Ld. CIT(A) had also deleted the addition of Rs. 5,54,161/- made on account of short changing of interest from associate concern. However, he sustained addition of Rs. 48,000/-.

4. Now the revenue is in appeal before the Tribunal. Apropos ground no. 1 of the appeal, which is against deletion of trading addition of Rs. 27,86,979/-. The Id. DR supported the order of the Assessing Officer and submitted that the Id. CIT (A) has passed a reasoned order. The Id. CIT(A), however, sustained the rejection of books of account against which the assessee has not been field any appeal. He submitted that where books of account have been rejected, the Assessing Officer is required to make estimation of the profit. He submitted that the Assessing Officer had examined the profit rate of preceding years. He submitted that Gross Profit rate during the year under consideration was lower than the Gross Profit rate declared by the assessee for the financial year 2008-09 and 2009-10. He submitted that the Assessing Officer had pointed out specific defects into the books of account. As observed by the Assessing Officer, some expenses debited by the assessee to Manufacturing/Trading Account were not verifiable since these were paid in cash and were supported only by vouchers prepared by the assessee. It was also observed that the explanation regarding disproportionate increase in expenses on Hexane, Fuel, Bardana & Packing Material was found to be only

partly satisfactory. Some purchases of mustard seeds had been made directly from farmers which was based upon self-made vouchers. He submitted that the Assessing Officer had pointed out method of valuation of closing stock of Mustard Cake, S.E. Soya Oil & SE Mustard Oil could not be verified since the assessee failed to file any documentary evidence. The Id. CIT(A) was not justified in estimating Gross Profit purely on the basis of conjectures despite the fact that the accounts as rejected, were sustained by Id. CIT(A).

5. On the other hand, the Id. AR of the assessee reiterated the submissions as made in the written brief. He submitted that law is well settled in making fair estimation, the Assessing Officer is required to take an exercise on all the direct evidence. He submitted that in the present case, the Assessing Officer had not made a fair estimation in conformity with the settled position of law. He submitted that past history of the case has been held to be the best guide for fair estimation. In this respect the Id. Counsel for the assessee has relied upon the judgment of the Hon'ble Rajasthan High Court rendered this case of CIT vs. Gupta K.N. Construction Co. (2015) 116 DTR 377 (Raj), Vaibhav Gems 112 DTR 84 (Raj). He submitted that from the comparative chart it is evident that there is a sharp increase in the turnover from 1.09 crore to 1.61 crore which is nearly 47% and for achieving increase in turnover. There is always compromise on margin in support of this contention, the Id. Counsel placed reliance on the judgment of the Hon'ble

Rajasthan High Court is the case of CIT vs. Amrapali Jewels (P) Ltd. (2012) 65 DTR 196 (Raj).

6. We have heard the rival contentions of both the parties, perused the material available on record and also gone through the orders of the authorities below. Admittedly, the rejection of books of accounts is not challenged by the assessee. The Id. CIT(A) has sustained the action of the Assessing Officer in respect of rejection of books of account. We find that the Id. CIT(A) has observed that the Assessing Officer had noticed certain shortcomings in the accounts and pointed them out to the assessee. It was further observed that the assessee was not able to detail variety bared pricing or justify clearly other deficiencies in maintaining properly vouched expenses related details tax packing materials, fuels etc. However, in respect of trading addition, the Id. CIT(A) did not agree with the Assessing Officer and observed as under:

"In the present case from the details of the facts brought on record, it is observed that the while the assessee's G.P. rate is lower as compared to 2 earlier preceding years, still it is higher than the immediately preceding year.

Hence considering the totality of facts involved and the fact that the A.O has reached his conclusion of estimating the G.P rate in this case merely by taking average of three years, I do not agree with the estimated increase in G.P rate to 4.30% in the Assessee's case as against 4.09% shown by the Assessee. No business can have a minimum threshold G.P every year just to satisfy the whims of the Assessing Officer, especially in this case where there is an increase in profit compared to the earlier year.

Looking to the totality of facts involved in the case, I would consider an addition of Rs. 5,00,000/- as justified towards increase in the G.P just on the basis of the discrepancies pointed out in the accounts, and not for any other reason. This would take the G.P rate up to 4.12%. The balance addition of Rs. 27,86,979/- is accordingly directed to be deleted.”

7. We are in agreement to the observations of the Id. CIT(A) where the books of account are rejected the Assessing Officer is required to make best judgment and this best judgment should be based on the material on record and after conducting through enquiry a fair and just estimate of profit should be deduced from the materials so placed before him. We find that the Id. CIT(A) sustained an addition of Rs. 5,00,000/- considering the fact that turnover had increased and also taking into consideration, the past history of the assessee qua the Gross Profit. He estimated. Gross Profit at 4.12 % which is lower than the Gross Profit of assessment year 2009-10 and 2008-09 where the Gross Profit was 5.13% and 5.34% respectively against turnover of Rs. 154.37 crores and 150.39 crores respectively. Under these facts. we are of the view that the Id. CIT(A) estimated at the lower side of the Gross Profit, it would be fair to adopt Gross Profit at 4.20%. The Id. Assessing Officer is directed to adopt which the Gross Profit at 4.20% and re-compute the trading addition accordingly. Thus ground No. 1 of Revenue’s appeal is partly allowed & Ground No. 2 is against deletion of addition of Rs. 1,00,000/-, made by involving the provisions of section 40A(2)(b) of the Act.

The Id. Counsel for the assessee reiterated the submissions made in written synopsis. On the contrary, Id. DR supported the orders of the Assessing Officer. He submitted Id. CIT(A) was not justified in deleting the addition.

8. We have heard rival contentions, perused the material available on record. We find Id. CIT(A) has decided the issue by observing as under:

“I have gone through assessee’s submission and AO’s findings. For disallowance u/s 40A (2)(b), the A.O. should have established that the payment to relatives is excessive compared to prevailing market rate. In this case it has not been done. The business results show vast upward movement, and considering the nature of the trade, the use of experience of the concerned relative cannot be denied. On a totality of facts, increase in the Salary of the concerned Director to the extent of Rs. 2,00,000/- is considered justifiable. The balance addition of Rs. 1,00,000/- is directed to be deleted.”

9. We find that admittedly, there is increase in turnover of the assessee company. Moreover, the Assessing Officer has not demonstrated as to how the salary paid is excessive to the Fair Market Value of the services rendered by the Director of the Company under this, which condition precedent for making such disallowance. Therefore, we do not see any infirmity in the order of the Id. CIT(A), same is hereby upheld.

10. Ground No. 3 is against the deletion of addition of Rs. 5,54,100/- made u/s 36(1)(iii).

11. On the other hand, the Id. DR supported the orders of the Assessing Officer and submitted Assessing Officer observed that the assessee has paid interest @ 12% per annum on loans taken from specified persons. However,

the assessee has charged interest @ 11% per annum only on the loans given to sister concerns i.e. M/s Shiv Edibles Ltd. & M/s Shiv Vegepro (P) Ltd. on the basis, the Assessing Officer made disallowance.

12. We have heard the rival contentions of both the parties, perused the material available on record and also gone through the orders of the authorities below. The Id. CIT(A) has given a finding on fact by observing as under:

I have gone through assessee's submissions and AO's findings.

"Since the issue involved in both the above Grounds relates to Interest allowability on borrowed funds as has been questioned by the AO in view of less rate or no interest charged by the assessee, these are being decided together.

The expressions "for the purpose of business" occurs in Section 36(1)(iii) and also in Section 37(1). A similar expression with different wording also occurs in Section 57(iii) which reads as "for the purpose of making or earning income". This issue came up for consideration before the Supreme Court and the Hon'ble Supreme Court while giving judgment in the case of Madhav Prasad Jatia v.CIT, (SC) 118 ITr 200 has established that the expression occurring in Section 36(1)(iii) is wider in scope than the expression occurring in Section 57(iii). Thus, meaning thereby that the scope for allowing a deduction under Section 36(1)(iii) would be much wider than the one available under section 57(iii).

This phrase, as held by many legal pronouncement, is the most important yardstick for the allowability of deduction u/s 36(1)(iii) of Income Tax Act, 1961. While explaining the meaning of this phrase the Hon'ble Supreme court in the case of S.A. Builders Ltd. Vs. CIT (A), Chandigarh reported in 288 ITR 1 has used the word "commercial expediency". It has been held in several judgments that by using this phrase Hon'ble Supreme Court has given a new dimension and clarified the concept further. In the judgment the Supreme Court has defined commercial expediency as "an expression of wide import and includes such expenditure as a prudent businessman incurs for the purpose of

business. The expenditure may not have been incurred under any legal obligation, but yet it is allowable as business expenditure, if it was incurred on grounds of commercial expediency". Further, following this judgment, the High Court of Delhi, in the case of Punjab Stainless Steel Inds. Vs. CIT 324 ITR 396, has further elaborated "The commercial expediency would include such purpose as is expected by the assessee to advance its business interest and may include measures taken for preservation, protection or advancement of its business interests, which has to be distinguished from the personal interest of its directors or partners, as the case may be. In other words, there has to be a nexus between the advancing of funds and business interest of the assessee-firm. The appropriate test in such a case would be as to whether a reasonable person stepping into the shoes of the directors/partners of the assessee-firm and working solely in the interest of the assessee-firm/company, would have extended such interest free advances. Some business objective should be sought to have been achieved by extending such interest free advances when the assessee/firm/company itself is borrowing funds for running its business".

Thus, for allowance of a claim for deduction of interest under this provision following three conditions are there:

(i) The money, that is capital, must have been borrowed by the assessee

(ii) It must have been borrowed for the purpose of business.

The assessee must have paid interest on the borrowed amount i.e. he has shown the same as an item of expenditure.

Proviso to Section 36(1)(iii)

The proviso to Section 36(1)(iii) was inserted by Finance Act, 2003 w.e.f. 01.04.2014 relating to A.Y 2004-05 and subsequent years. This was inserted to disallow interest on moneys borrowed for acquiring a capital asset till the date on which the asset was brought to use even if it is for extension of existing business. Following facts are important for consideration.

This proviso is to operate prospectively as held by Hon'ble Supreme Court in the case of Deputy Commissioner of Income Tax. Vs. Core Health Care Ltd. (SC) 298 ITR 194.

In this proviso, the word "extension" has been used which is to be taken as synonymous to the word "expansion" which is used for Sections 801C(8)(ix) and 801E(7)(iii)[as held in case of Nahar Poly Films Ltd. Vs. CIT, Ludhiana 201 Taxman 304 (P&H)]. The word expansion is not different from extension of business and therefore the interest expenditure, on the utilization of borrowed funds for the

acquisition of new assets, from the date of its acquisition till the date when the asset is put to use, is to be disallowed.

Expenditure may either relate to a new unit on expansion of existing business or it may relate to a totally new business apart from existing business.

Hon'ble Supreme Court has brought out the following interpretations:

1. Section 36(1)(iii) has to be read on its own terms. It is a code by itself. Section 36(1)(iii) is attracted when the assessee borrows the capital for the purpose of his business. It does not matter whether the capital is borrowed in order to acquire a revenue asset or a capital asset, because all that the section requires is that the assessee must borrow the capital for the purpose of his business. There by meaning that the transaction of borrowing is not the same as the transaction of investment.
2. Explanation 8 to Section 43(1) has not relevance to Section 36(1)(iii). It has relevance only to Sections 32,32A, 33 and 41 which deal with concepts like depreciation.
3. The provisions under section 36(1)(iii) make no distinction between money borrowed to acquire a capital asset and a revenue asset.

Under the circumstances of the case and the legal interpretations available, it can be held that not only did the assessee use the borrowed funds for business purposes but did also have sufficient other interest free funds available for investments carried out for long term business prospects. The AO has not been able to prove anything to the contrary by bifurcating the interest bearing considerations involved or prudence and make notional disallowance. The case law of *Abhishek Industries Vs. CIT, Ludhiana (2006)* which used to be relied in such issues by various assessing officers has been overruled in *Munjal Sales Corporation vs. CIT, Ludhiana 168 Taxman 42 (SC)*

As a result the addition of Rs. 5,54,161/- made on account of short charging of interest from associate concern cannot be sustained. The same is directed to be deleted."

13. The Assessee has sufficient other interest free funds available for investment carried for long term business. Assessing Officer was not able to

prove anything to the contrary by bifurcating the interest bearing and free funds and their respective use. This finding of fact is not rebutted by the revenue by placing any contrary material on record. We do not see any infirmity in the order of the Ld. CIT(A). As it is not disputed that the assessee has sufficient interest free funds available for advancing money to sister concerns. Hence this ground is dismissed.

14. Ground No.4 of the Revenue's appeal is general in nature and hence, requires no specific adjudication.

15. In the result, appeal of the revenue is partly allowed.

Order pronounced in the open court on 23/05/2017.

Sd/-
(भागचन्द)
(BHAG CHAND)
लेखा सदस्य/Accountant Member

Sd/-
(कुल भारत)
(KUL BHARAT)
न्यायिक सदस्य/Judicial Member

Jaipur

Dated:- 23/05/2017

Ganesh Kumar

आदेश की प्रतिलिपि अग्रेषित/Copy of the order forwarded to:

1. The Appellant- Assistant Commissioner of Income Tax, Kota
2. The Respondent – M/s Shiv Agrevo Ltd., Baran
3. The CIT(A).
4. The CIT,
5. The DR, ITAT, Jaipur
6. Guard File (ITA No. 453/JP/2016)

आदेशानुसार/ By order,

सहायक पंजीकार/ Assistant. Registrar