

**IN THE INCOME TAX APPELLATE TRIBUNAL "G" BENCH, MUMBAI  
BEFORE G.S.PANNU, AM AND SHRI RAVISH SOOD, JM**

ITA No. 476/Mum/2015  
(निर्धारण वर्ष / Assessment Year:2009-10)

Gurera Synthetics Pvt. Ltd., 33/37 Dwarkesh Market, Dr. A.M. Road, Bhuleshwar, Mumbai 400 002	<b>बनाम/ Vs.</b>	Income Tax Officer 4(2)(3) Aaykar Bhavan, M.K. Road, Mumbai 400020
स्थायी लेखा सं./जीआइआर सं./PAN No. AAACG2269G		
(अपीलार्थी / <b>Appellant</b> )	:	(प्रत्यर्थी / <b>Respondent</b> )

अपीलार्थी की ओर से / <b>Appellant by</b>	:	Shri Narayan Atal, A.R
प्रत्यर्थी की ओर से / <b>Respondent by</b>	:	Shri V. Vidyadhar, D.R

सुनवाई की तारीख / <b>Date of Hearing</b>	:	13.10.2017
घोषणा की तारीख / <b>Date of Pronouncement</b>	:	08.11.2017

**आदेश / ORDER**

**PER RAVISH SOOD, JUDICIAL MEMBER:**

The present appeal is directed against the order passed by the CIT(A)-8, Mumbai, dated 03.11.2014, which in itself arises from the assessment order passed by the A.O u/s 143(3) r.w.s. 147 of the Income tax Act, 1961, (for short 'Act'), dated 15.03.2013. The assessee assailing the order of the CIT(A) had raised before us the following grounds of appeal:-

*“Being aggrieved by the order of CIT(A)18, Mumbai this appeal petition is being submitted on the following grounds each of which, it is prayed, be considered independently without prejudice to one another:*

- 1. In the facts and circumstances of the case and in law, the learned CIT(A) erred in upholding assessing Officer's (A.O's) action in disallowing Manufacturing & other expenses of Rs.45,740/-.*
- 2. In the facts and circumstance of the case and in law, the learned CIT(A) erred in upholding Assessing Officer's (A.O's) action in disallowing Rs.12,71,140/- out of selling & administrative expenses.*
- 3. In the facts and circumstances of the case and in law, the learned CIT(A) erred in not adjudicating on the disallowance of electricity expenses at Rs.3,50,000/- as against the electricity expenses of Rs.3826/- claimed by the appellants.*
- 4. In the facts and circumstances of the case and in law, the learned CIT(A) erred in upholding Assessing Officer's (A.O's) action in disallowing Rs.1,80,500/- u/s 40A(3) being remuneration paid to Ravi Arya, the Director of the company.*
- 5. In the facts and circumstances of the case and in law, the learned CIT(A) erred in upholding Assessing Officers (A.O's) action in disallowing interest on term loan of Rs. 4,77,923/- u/s 36(1)iii).*
- 6. In the facts and circumstances of the case and in law, the learned CIT(A) erred in upholding Assessing Officer's (A.O's) action in disallowing security charges of Rs. 1,03,862/- u/s 40(a)(ia) paid to Chauvan Detective Security Services.*
- 7. In the facts and circumstances of the case and in law, the learned CIT(A) erred in upholding Assessing Officers (A.O's) action in disallowing employees contribution to ESIC of Rs.898/- u/s 2(24)(x) r.w.s 36(1)(va).*
- 8. Your appellants craves leave to add to, amend, alter, delete and/or modify the above grounds of appeal on or before the final date of hearing.”*

2. Briefly stated, the facts of the case are that the assessee company which is engaged in the business of dyeing and processing of textiles had filed its return of income declaring total income for A.Y. 2009-10 at Rs. Nil on 28.10.2009. The return of income filed by the assessee was processed as such u/s 143(1) of the 'Act'. The case of the assessee was reopened by the A.O for the reason that during the course of the scrutiny proceedings in the case of the director of the assessee company, viz. Shri S.R. Arya for A.Y. 2009-10, it was gathered that the assessee company had paid cash salary of Rs. 5,30,000/- to its directors Shri S.R. Arya and Smt. Ravi Arya, on which no tax was deducted at source.

3. That during the course of the assessment proceedings it was observed by the A.O that though the assessee had accounted for miscellaneous income of Rs.1,41,83,149/- by way of (i) writing off of the balance outstanding against a sundry creditor; (ii) interest on security deposits with MIDC and MSED; and (iii) insurance claim received by the assessee, but however, no manufacturing activity was carried out by the assessee during the year. The A.O holding a conviction that now when no manufacturing activity was carried out by the assessee during the year under consideration, therefore, the expenses claimed by it in the profit and loss account could not be allowed. The A.O called upon the assessee to put forth an explanation as regards the allowability of the said expenses. The assessee in its explanation submitted before the A.O that there were manifold factors due to which no manufacturing activity could be carried out during the year under consideration, viz. (i) the assessee had suffered a substantial loss in its business, as a result whereof during the year it remained in a deep financial crisis; (ii) the debtors were not forthcoming with the outstanding balances, as a result whereof the finances of the assessee got stuck; and (iii) the bankers of the assessee had declined to provide finances and had rather characterised the bank account of the assessee as a Non-performing asset. The assessee submitted before the A.O that though during the year under consideration due to the aforesaid compelling circumstances the manufacturing activities could not be carried out and its plant remained closed, but however, it remained as a matter of fact that the assessee had not shut down its business. That in the backdrop of the aforesaid facts it was further averred by the assessee that as the expenses which were claimed in the profit and loss account were fixed expenses which had been incurred wholly and exclusively in the course of its business, therefore, the same had rightly been claimed

while computing its income. The assessee in order to drive home its aforesaid contention that the company had not shut down its business, submitted before the A.O that in the subsequent years the assessee was able to wriggle out of the financial crisis and had continued with its business operations and generated substantial profits. Thus, in the backdrop of the aforesaid contentions it was submitted by the assessee that the expenses debited in the profit and loss account were rightly claimed while computing the income for the year under consideration.

4. However, the A.O after deliberating on the contentions of the assessee did not find favour with the same. The A.O holding a conviction that as the assessee had not carried out any manufacturing activity during the year under consideration, therefore, for the said reason disallowed certain expenses which were claimed by the assessee in its profit and loss account along with certain other additions/disallowances, as under:-

Sr. No.	Particular	Amount
1.	Disallowance of manufacturing and other expenses.	Rs. 45,470/-
2.	Disallowance out of Selling and administrative expenses	Rs.12,71,140/-
3.	Disallowance of Salary paid to directors of the assessee company	Rs.1,80,500/-
4.	Disallowance of Interest on term loan u/s 36(1)(iii)	Rs.4,77,923/-
5.	Disallowance of security charges u/s 40(a)(ia)	Rs. 103,862/-
6.	Disallowance of employees contribution to ESI u/s 2(24)(v)	Rs. 989/-

	r.w.s. 36(1)(va)	
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The A.O after making the aforesaid disallowance/additions assessed the income of the assessee at Rs.66,69,330/-, vide his order passed u/s 143(3) r.w.s. 147 of the Act, dated 15.03.2013.

5. Aggrieved, the assessee carried the matter in appeal before the CIT(A). The CIT(A) after deliberating on the contentions of the assessee in the backdrop of the facts of the case upheld the aforesaid disallowance/additions made by the A.O and partly allowed the appeal of the assessee.

6. The assessee being aggrieved with the order of the CIT(A) had carried the matter in appeal before us. The Id. Authorized Representative (for short A.R) for the assessee submitted that the assessee being in a financial crisis on account of manifold factors, viz. (i) the assessee had suffered a substantial loss in the past as a result whereof it was in a financial crisis during the year; (ii) that as the debtors were not forthcoming with the outstanding balances, therefore, the finances of the assessee were stuck; and (iii) the bankers of the assessee had also declined to provide finances and had characterised the bank account of the assessee as a Non-performing asset account, coupled with the fact that there was a lull in the business during the year under consideration, had thus not carried out any manufacturing activity during the said year. It was however submitted by the Id. A.R that it had not closed down its business, which in itself stood substantiated from the very fact that the assessee had carried out business and generated substantial profits in the succeeding years. The Id. A.R in order to fortify his aforesaid contention therein drew our attention to Page 14 of his 'Paper book' (for short 'APB'), which revealed the substantial sales of the assessee

for the succeeding years, viz. Financial year 2009-10 to 2015-16. It was submitted by the Id. A.R. that the lower authorities had gravely erred in assuming that the assessee had closed down its business. Per contra, the Id. D.R relied on the orders of the lower authorities.

7. We have heard the authorized representatives for both the parties, perused the orders of the lower authorities and the material available on record. We have given a thoughtful consideration and are persuaded to be in agreement with the contention of the Id. A.R that though the assessee due to serious financial constraints and other compelling circumstances was unable to carry out its manufacturing activities during the year, but it had never closed its business. We have perused the sales of the assessee for the succeeding years and find that the assessee had carried out substantial sales, which fact in itself dislodges the observations of the authorities below that the assessee had closed its business. We thus, on the basis of our aforesaid observations proceed with and adjudicate the validity of the additions/disallowances which had been sustained by the CIT(A) and assailed by the assessee before us.

8. The Id. A.R at the very outset had assailed the disallowance of manufacturing and other expenses of Rs. 45,740/- made by the A.O. We find that the aforesaid disallowance made by the A.O had thereafter been sustained by the CIT(A), for the reason that no manufacturing activity was carried out by the assessee during the year under consideration. We are unable to persuade ourselves to accept the aforesaid observations of the CIT(A). We are of the considered view that the test for allowability of an expenditure in terms of Section 37(1) is that the expenditure should not be found to be in the nature of a capital expenditure or by way of personal expenses of the assessee, and must have been laid out or expended

wholly and exclusively for the purposes of the business of the assessee. We find that as observed by us hereinabove, the business of the assessee had not been closed, but rather, only due to recession and financial constraints the assessee could not carry out the manufacturing activity during the year. We find that as the aforesaid expenditure had been incurred wholly and exclusively for the purpose of the business of the assessee and is not found to be in the nature of capital expenditure or a personal expense of the assessee, therefore, the same is allowable as per the provisions of Section 37(1) of the Act. We thus in light of our aforesaid observations set aside the disallowance of Rs.45,740/- which had been sustained by the CIT(A).

**The Ground of the appeal no. 1** is allowed.

9. The assessee had further assailed the disallowance of Rs.12,71,140/- pertaining to selling and administrative expenses, which had been sustained by the CIT(A). The ld. A.R before adverting to his contentions in context of the allowability of the aforesaid expenses, took us through Page 2-3 of the 'APB' and submitted that the assessee had under the aforesaid head of expense booked 'electricity charges' of Rs.3,826/- only, but the A.O had wrongly taken the same at an amount of Rs.3,50,000/- while computing the aggregate of the aforesaid expenses at Rs.12,71,140/-. The ld. A.R in order to fortify his aforesaid contention took us to Page 3 of the assessment order. The ld. A.R further assailed the addition/disallowance made by the A.O and averred that now when the business of the assessee was not closed, therefore, there was no reason as to why the said expenses which had wholly and exclusively been incurred by the assessee for the purpose of its business were not to be allowed. We have given a thoughtful consideration to the aforesaid addition/disallowance of Rs.12,71,140/- made by the A.O in

respect of selling and administrative expenses. We find that the aforesaid additions/disallowance had been sustained by the CIT(A), for the reason that as no manufacturing activity was carried out by the assessee during the year under consideration, therefore, the aforementioned expenses claimed by the assessee were to be taken as not having been incurred wholly and exclusively for its manufacturing activity, and could not be allowed as an expenditure for computing of its income. We are unable to find ourselves as being in agreement with the aforesaid view of the CIT(A). We are of the considered view that for allowability of expenses under Sec.37(1), the pre-requisite condition is that the same should have been laid out or expended wholly and exclusively for the purpose of the business of the assessee. We have deliberated on the nature of the aforesaid expenses (Page 3 of the 'APB') and are of the considered view that all of the expenses booked under the aforesaid head of expense are clearly found to have been incurred by the assessee wholly and exclusively for the purpose of its business. We are of the view that as the business of the assessee had not been closed during the year, therefore, the disallowance of the aforesaid expenses which are found to have been incurred wholly and exclusively for the purpose of the business and not in the nature of capital expenditure or personal expenses of the assessee, are thus, allowable while computing the income of the assessee for the year under consideration. We thus, in the backdrop of our aforesaid observations delete the disallowance of Rs.12,71,140/- which had been sustained by the CIT(A). Before parting, we may herein observe that a perusal of the bifurcated details of the selling and administrative expenses furnished by the assessee (Page 3 of 'APB') reveals that the A.O while computing the said expenses at an amount of Rs.12,71,140/- had wrongly taken the figure of the electricity charges at Rs.3,50,000/-, which we find had been claimed by the

assessee at an amount of Rs.3,826/-. However, as we have already deleted the additions/disallowance of Rs.12,71,140/- in terms of our aforesaid observations, therefore, our observations as regards the mistake in adopting the amount of the electricity expenses would be rendered as academic. **The Ground of appeal No. 2 and 3** are allowed in terms of our aforesaid observations.

10. The assessee had further assailed the disallowance u/s 40A(3) of the remuneration of Rs.1,80,500/- paid by the assessee company to its directors Mrs. Ravi Arya, which thereafter had been upheld by the CIT(A). We find that the assessee had during the year under consideration made a monthly payment of Rs.15,000/- to its director Mrs. Ravi Arya, as a result whereof an aggregate payment of Rs.1,80,000/- (i.e. @ Rs.15,000/- p.m.) was made to the director during the year. We find that the A.O invoking the provision of Sec. 40A(3) had disallowed the amount of Rs.1,80,000/-.

11. We are of the considered view that as per the mandate of Section 40A(3) (as was available on the statute during the year under consideration, viz. AY: 2009-10) it was obligatory on the part of the assessee to make a payment of a sum exceeding Rs.20,000/- only by way of an account payee cheque drawn on a bank or account payee bank draft, failing which the said expenditure was liable to be disallowed. We find that the remuneration paid by the assessee to its director Mrs. Ravi Arya was Rs.15,000/- per month, which was below the limit of Rs.20,000/- contemplated under Section 40A(3), therefore, no disallowance on the said count was called for in the hands of the assessee. We thus, on the basis of the details of the respective monthly payments made by the assessee to its director Mrs. Ravi Arya during the year under consideration (placed on record by the assessee), delete the disallowance of Rs.1,80,000/- under Section

40A(3), which had been sustained by the CIT(A). **The Ground of appeal no. 4** is allowed.

12. The assessee had further assailed before us the sustaining by the CIT(A) of the disallowance under Sec. 36(1)(iii) of interest of Rs.4,77,423/- paid by the assessee on term loan. That during the year under consideration there was a 'debit balance' of Rs.45,51,645/- appearing in the current account of the director in the books of account of the assessee. The A.O observed that the assessee had during the year under consideration borrowed interest bearing funds and had paid interest of Rs.18,91,450/- on the term loan which was raised by it from SIDBI. The A.O noticed that the assessee had diverted part of the said interest bearing funds by advancing an interest free loan of Rs.45,51,645/- to its director Shri Satyapriya R. Arya. The A.O being of the view that as the assessee had paid interest at the rate of 10.5% on the term loan, therefore, the utilization of the aforesaid interest bearing funds for non business purposes, i.e by advancing the same free of interest as a loan to its director would call for a disallowance of the correlating interest u/s 36(1)(iii). The A.O on the basis of his aforesaid conviction disallowed interest of Rs.4,77,923/- (i.e. at the rate of 10.5% P.A. on the loan amount of Rs.45,51,645/-) u/s 36(1)(iii), which on appeal was sustained by the CIT(A).

13. We have deliberated on the facts pertaining to the issue under consideration and are unable to persuade ourselves to accept the observations of the lower authorities. We find that the assessee had submitted before both of the lower authorities that as it had total interest free funds of Rs.199.72 lacs available with it during the year, therefore, the same sufficiently explained the source of the debit balance of Rs.45,51,645/- appearing in the current account of the

director of the assessee company during the year under consideration. It was thus the contention of the assessee before the lower authorities, that now when there were sufficient interest free funds available with it, therefore, no disallowance in respect of the aforesaid amount was called for u/s 36(1)(iii) in the hands of the assessee. We find that the assessee in support of its contention had specifically relied on the judgment of the **Hon'ble High Court of Bombay** in the case of **CIT Vs. Reliance Utilities and Power Ltd. (2008) 313 ITR 340 (Bom)**. We find that the CIT(A) sustained the disallowance of interest on borrowed capital for the reason, that as the borrowed funds of the assessee of Rs.4,05,51,293/- were more than its self owned funds of Rs.2,10,58,442/-, therefore, as per him it could safely be concluded that the borrowed funds had been utilized by the assessee for giving interest free loan to the director.

14. We are unable to subscribe to the aforesaid view of the CIT(A). We are of the considered view that the Hon'ble High Court of Bombay in the case of Reliance Utilities and Power Ltd. (supra) had very clearly held that where an assessee is having sufficient self owned funds, no disallowance under Sec. 36(1)(iii), to the extent such funds are available, would be called for in the hands of the assessee. We thus, in the backdrop of the aforesaid facts and the settled position of law are of the considered view that now when the assessee had sufficient self owned funds of Rs.2,10,58,442/-, therefore, it could safely be concluded that no disallowance u/s 36(1)(iii) in respect of interest on borrowed capital pertaining to the 'debit balance' of Rs.45,51,645/- appearing in the current account of the director of the assessee company was called for in the hands of the assessee. We thus delete the disallowance of Rs.4,77,923/- which had been sustained by the CIT(A). **The Ground of appeal no. 5** is allowed.

15. The assessee had further assailed before us the disallowance made u/s 40(a)(ia) of Rs.1,03,862/- in respect of the security charges which were paid by the assessee to M/s Chouvan Detective Securities Services during the year under consideration. We find that the assessee had submitted before the CIT(A) that as the said amount was 'Paid' to the aforementioned payee during the year itself, and as such was not 'Payable' at the end of the year, therefore, in view of the order of the **ITAT, Vishakhapatnam 'Special bench'** in the case of **Merilyn shipping & Transport Vs. Addl. CIT. (2012) 136 ITD 23 (SB)** no disallowance under the aforesaid statutory provision was called for in the hands of the assessee. We further find that the assessee had also relied on the judgment of the **Hon'ble High Court of Allahabad** in the case of the **CIT Vs. Vector Shipping Pvt. Ltd. (2013) 357 ITR 642 (All)**. We are of the considered view that the **Hon'ble Supreme Court** in the case of **Palam Gas Service Vs. CIT (2017) 394 ITR 300 (SC)** had recently held that Section 40(a)(ia) covers not only those cases where the amount is payable, but also where the amounts which had been paid. Thus, in the backdrop of the aforesaid judgment of the Hon'ble Apex Court, where an assessee in terms of Sec. 40(a)(ia) is found to had failed to comply with the TDS provisions in respect of an expense claimed by him while computing its income, the said amount of expense, irrespective of the fact as to whether the same had been paid or is payable, would be disallowed in the hands of the assessee. We are of the considered view that after the aforesaid judgment of the Hon'ble Supreme Court the issue remains no more *res integra*, and the order/ judgment so relied upon by the assessee does not hold the ground any more. We thus, in the backdrop of our aforesaid observations uphold the disallowance of Rs.1,03,862/- made by the A.O u/s 40(a)(ia), which thereafter had been sustained by the CIT(A).

16. The assessee had further assailed before us the disallowance of the employees contribution to ESIC of Rs.989/- u/s 2(24)(x) r.w.s. 36(1)(va). We find that the A.O being of the view that as the assessee had deposited the employees contribution to ESIC fund beyond the 'due date' by which he as an employer was required to deposit the same in the employees account with the relevant fund, therefore, disallowed the same. That on appeal the CIT(A) confirmed the said addition/disallowance. The CIT(A) observed that the deletion of the *second proviso* to Sec. 43B and the amendment made available on the statute vide the Finance Act, 2003 was required to be confined to Sec. 43B alone. The CIT(A) further observed that the deletion of the *second proviso* to Sec. 43B by the amendment pursuant to the Finance Act, 2003, could not be made applicable w.r.t Sec. 36(1)(va) of the 'Act'. Thus, the CIT(A) being of the considered view that the assessee would be entitled towards deduction in respect of employees contribution to the ESIC fund, provided the sum is credited by the assessee in the accounts of the concerned employees and in the concerned funds on or before the 'due date' under the Employees State Insurance Act, Rules, Order or Notification issued there under or under any standing order, award, contract or service or otherwise. The CIT(A) on the basis of his aforesaid observations being of the view that the deposit of the amount by the assessee in the ESIC fund was not within the 'due date' contemplated under the ESI Act, therefore, upheld the addition/disallowance made by the A.O.

17. We have deliberated on the issue under consideration and at the first blush find the observations of the CIT(A) to be convincing and well in order. However, we have deliberated on the issue under consideration and find that though the amount of the employees contribution towards ESIC was deposited by the assessee in the

concerned fund beyond the 'due date' contemplated under the Employees State Insurance Act/Rules, however, the same having been deposited well before the 'due date' of filing of the return of income by the assessee, therefore, the same in the backdrop of the judgment of the **Hon'ble High Court of Bombay** in the case of **CIT Vs. Ghatge Patil Transports Ltd. (2014) 368 ITR 0749 (Bom)** wherein it has been held that both the employers and employees contributions towards the employees welfare funds would be covered by the amendment made to Sec. 43B vide the Finance Act, 2003, therefore, hold that the aforesaid amount of Rs. 989/- pertaining to the employees contribution to the ESIC, though deposited by the assessee beyond the 'due date' contemplated under the ESI Act/Rules, but well within before the 'due date' for filing of the return of income by the assessee, would thus be allowable as a deduction. We thus, in the backdrop of our aforesaid observations set aside the order of the CIT(A) and delete the disallowance of Rs. 989/-. The **Ground of appeal no. 7** is allowed. The **Ground of appeal no. 8** being general in nature is dismissed as not pressed.

17. The appeal of the assessee is partly allowed in terms of our aforesaid observations.

Order pronounced in the open court on 08.11.2017

Sd/-  
(G.S. Pannu)  
Accountant Member  
मुंबई Mumbai;दिनांक 08.11.2017

Sd/-  
(Ravish Sood )  
Judicial Member

**आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :**

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent.
3. आयकर आयुक्त(अपील) / The CIT(A)-
4. आयकर आयुक्त / CIT
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, मुंबई /  
DR, ITAT, Mumbai
6. गार्ड फाईल / Guard file.

सत्यापित प्रति //True Copy//

आदेशानुसार/ BY ORDER,  
उप/सहायक पंजीकार (Dy./Asstt. Registrar)  
आयकर अपीलीय अधिकरण, मुंबई / **ITAT,**  
**Mumbai**