

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

श्री कुल भारत, न्यायिक सदस्य एवं श्री विक्रम सिंह यादव, लेखा सदस्य के समक्ष
BEFORE: SHRI KUL BHARAT, JM & SHRI VIKRAM SINGH YADAV, AM

आयकर अपील सं./ ITA No. 137/JP/17
निर्धारण वर्ष / Assessment Year : 2013-14

Bajargan Traders C/o Kalani & Co., CA, 5 th Floor , The Mile stone , Gandhi Nagar Turn, Tonk Road, Jaipur	बनाम Vs.	The ACIT, Circle-2, Alwar
स्थायी लेखा सं./ जीआईआर सं./ PAN No. AABFB 2413 K		
अपीलार्थी / Appellant		प्रत्यर्थी / Respondent

निर्धारिती की ओर से / Assessee by : Shri P.C. Parwal (C. A)
राजस्व की ओर से / Revenue by : Shri Prem Prakash Meena (JCIT)

सुनवाई की तारीख / Date of Hearing : 14.03.2017
घोषणा की तारीख / Date of Pronouncement : 17/03/2017.

आदेश / ORDER

PER SHRI VIKRAM SINGH YADAV, A.M.

This is an appeal filed by the assessee against the order of Ld. CIT(A), Alwar dated 05.01.2017 wherein the assessee has taken following two grounds of appeal:

“(1). *The ld. CIT(A) has erred on facts and in law in confirming the addition of Rs. 70,04,814/- (wrongly mentioned as Rs. 57,46,980/-) on account of excess stock found during the survey by wrongly stating that assessee has backtracked from the statement given in course of search and by ignoring that assessee has himself credited the income on account of excess stock found in survey in the Profit and Loss Account and thus, offered such excess stock found in survey for tax. He has further erred in not considering that:*

- (a) *the excess stock found in survey is to be assessed under the head "Profits and Gains from Business" as offered by the assessee as against "Income from other Sources" assessed by the AO.*
- (b) *AO arrived at the profits of the business at Rs. 1,08,55,878/- by determining the credit to the Trading & Profit and Loss Account (excluding undisclosed stock amount) at Rs. 35,46,85,308/- and reducing there from the total of purchase and other expenses (excluding undisclosed stock amount) at Rs. 34,38,29,430/- but in that process not reducing the amount of Rs. 70,04,814/- credited by the assessee to the Trading & Profit and Loss Account which is separately assessed by him as "income from Other Sources" thus resulting into double addition.*
- (2.) *The Id. CIT(A) has erred on facts and in law in disallowing the interest expenses of Rs. 1,39,366/- on the ground that the advance is given to Smt. Rita Gupta at interest rate of 10% whereas assessee has paid interest on the borrowed funds @ 14% whereas the AO has made this addition on account of notional interest.*

2. Regarding Ground No. 1, the facts of the case are that during the year under consideration, a survey u/s 133 of the Act was conducted at the business premises of the assessee on 08.11.2012. During the survey operation, the assessee has surrendered an amount of Rs. 70,04,814/- on account of a major discrepancy in stock of rice which had hitherto not been recorded in books of accounts. Further, the partner of the assessee firm admitted that the investment had been made out of undisclosed sources. The due tax amount has been paid by the assessee on such undisclosed amount of stock. On perusal of Note on accounting policy filed alongwith audit report, it was noticed by the AO that "a major discrepancy in stock of rice of Rs. 70,04,814/- was observed during the course of survey which was offered for taxation as arised on account of income from undisclosed sources and during the year under audit, account of the assessee reflects this transaction as debiting purchase account and crediting the undisclosed income by Rs.70,04,814/-".

2.1 The assessee was thereafter issued a show-cause stating that the assessee firm has taken the double benefit of undisclosed income surrendered during survey operation in the following manner:

“The assessee has credited the Trading and Profit and Loss account by taking the amount of undisclosed income to the credit side, while on the other hand, the assessee has debited the same amount and clubbed it with purchases made during the year. In the result, the assessee has reduced its tax liability by doing so. During the survey operation, the excess stock of rice Rs.70,04,814/- which was its investment from undisclosed sources and has to be taxed under the head of income from other sources exclusively. It is not part of trading and profit and loss account. Further the assessee was asked to explain as to why the purchases should not be reduced by Rs. 70,04,814/-.”

2.2 In response to the show-cause, the assessee submitted that it trades in rice and that the inclusion of the amount of undisclosed investment in purchases shall not result in decline in GP ratio. The contention of the assessee was however not accepted by the AO. As per AO, if the assessee is allowed to include the amount of undisclosed investment in stock in both credit as well as debit side of the Trading and Profit & Loss account, it negates the entire purpose of such surrender during survey and the correct treatment shall be to treat the amount of surrendered undisclosed investment in stock as income under the head “other sources” exclusively. Thus the amount was excluded from the Trading and Profit and Loss account and was taxed under the head “income from other Sources”.

2.3 Being aggrieved, the assessee carried the matter in appeal before the Id CIT(A). The findings of the Id. CIT(A) is reproduced as under:

“I have considered the above mentioned facts. I have also noted the fact that appellant has further included the amount of Rs.70,04,814/- both the credit side and debit side, thereby negating the impact of this excess stock to naught. Furthermore , I have also perused the statement given by the appellant during the course of survey operation where in response to the question No. 30 with regard to excess stock valued at Rs.70,04,814/- he has categorically stated that the amount reflects the undisclosed investment he has made in the stock and offered for taxation. Not only this, in response to question No. 31 & 32 with regard to slips found and impounded as per Annexure A with regard to unaccounted sales”, he has evaded the reply which ultimately suggests that such loose sheets reflected the generation of unaccounted income which ultimately is used for the investment made in the unaccounted purchase of excess stock. In view of these facts, it is my considered view that the AO has rightly added the amount of Rs. 70,04,814/- as surrendered amount on account of excess stock which has been accepted by the appellant as his investment. Therefore, there is no reason to backtrack from the statement given by the appellant during survey operation about the undisclosed investment of Rs. 70,04,814/-. Hence the addition of Rs. 57,46,980/- is sustained. Accordingly appellant’s ground of appeal on this issue is dismissed.”

2.4 Now the assessee is in appeal against the order of the Id CIT(A). In this regard, the Id. AR has submitted that the assessee is a partnership firm dealing in sale of food grain, rice and oil seeds. A survey u/s 133A was conducted on the business premises on 08.11.2012. During the survey, assessee surrendered excess stock of rice amounting to Rs. 70,04,814/-. In the profit and Loss

account, the amount so surrendered is credited as income from undisclosed sources and after claiming deduction on account of interest/remuneration to partners, return declaring income of Rs. 43,36,920/- was filed on 28.09.2013.

2.5 It was submitted by the Id AR that both the lower authorities have not appreciated the facts in correct perspective. This is because the assessee in the audited profit & loss account has debited the undisclosed investment in stock in purchase account and simultaneously it has become part of sales/closing stock in the credit side, nullifying the effect of the same. Therefore, the undisclosed investment in stock is separately credited in the profit and loss account under the head "income from undisclosed sources". It is for this reason that the net profit without considering remuneration to partners as per the audited profit & loss account is Rs.1,08,55,878/- (APB 23). If this amount is excluded both from purchase and the closing stock, then also the net profit remains the same (APB 24). Had this amount not credited separately to the profit & loss account the net profit without considering the remuneration to partners would have been only Rs.39,35,632/- (APB 25). Thus, it is clear that assessee has separately offered the undisclosed investment in stock found in survey as business income. It would not make any difference to the total income whether it is offered under the head 'business income' or under the head 'income from other sources'.

2.6 It was further submitted that the AO has made incorrect calculation at Para 4 of the assessment order. This is because, though he has reduced the amount of Rs.70,04,814/- from both the debit side and the credit side, he failed to consider that though this amount is a part of the sales/closing stock, assessee has further credited this amount in the profit and loss account. Therefore, he ought to have further reduced this amount from the credit side

of the profit and loss account, once he intended to include it under the head income from other sources. Not excluding the same has resulted into double addition of the same amount in as much as it has remained as a part of the income under the head business and again assessed by him as income from other sources. Hence, the income assessed by the AO under the head profit & gains of business at Rs. 42,86,178/- is erroneous. The Ld. CIT(A) also wrongly observed that the assessee has backtracked from his statement ignoring that this amount is already offered to tax by the assessee separately.

2.7 It is further submitted that the real issue in this case is whether the excess stock surrendered should be made as a part of business income or not and if so, assessee can claim deduction on account of payment of remuneration to partners on account u/s 40b(v). In this regard, our reference was drawn to the decision of Co-ordinate Bench in case of **Shri Ramnarayan Birla** (in ITA No. 482/JP/15 dated 30.09.2016). In that case, the question before the Coordinate Bench was “whether the CIT(A)-2, Udaipur has erred in directing the AO to assess the unexplained investment surrendered by the assessee under the head “Income from Business” ignoring the decision of the Hon’ble Gujarat High Court in the case of Fakir Mohd. Hazi Hasan 247 ITR 290 that unaccounted income ought to be categorized under the residuary head of ‘Income from other sources”. In respect to the said issue, the findings of the Coordinate Bench are as follows:

“ We have heard the rival contentions and perused the material available on record. Undisputed facts emerged from the record that at the time of survey excess stock was found. It is also not disputed that the assessee is engaged in the business of jewellery. During the course of survey excess stock valuing Rs. 77,66,887/- was found in respect of gold and jewellery. The Coordinate Bench in the case of Choksi Hiralal Maganlal vs. DCIT 131, TTJ (Ahd.)¹ has held that

in a cases where source of investment/expenditure is clearly identifiable and alleged undisclosed asset has no independent existence of its own or there is no separate physical identity of such investment /expenditure then first what is to be taxed is the undisclosed business receipt invested in unidentifiable unaccounted asset and only on failure it should be considered to be taxed u/s 69 on the premises that such excess investment is not recorded in the books of account and its nature and source is not identifiable. Once such excess investment is taxed as undeclared business receipt then taxing it further as deemed income under section 69 would not be necessary. Therefore, the first attempt of the assessing authority should be to find out link of undeclared investment/expenditure with the known head, give opportunity to the assessee to establish nexus and if it is satisfactorily established then first such investment should be considered as undeclared receipt under that particular head. It is observed that there is no conflict with the decision of Hon'ble Gujarat High Court in the case of Fakir Mohd. Hajihasan (supra) where investment in an asset or expenditure is not identifiable and no nexus was established then with any head of income and thus was not available for set off against any loss under any other head. Therefore, the Hon'ble Coordinate Bench held that where asset in which undeclared investment is sought to be taxed is not clearly identifiable or does not have independent identity but is integral and inseparable (mixed) part of declared asset falling under a particular head, then the difference should be treated as undeclared business income explaining the investment. In the present case the excess stock was part of the stock. The revenue has not pointed out that the excess stock has any nexus with any other receipts. Therefore we do not find any fault with the decision of the Ld. CIT(A) directing the AO to treat the surrendered amount as excess stock qua the excess stock found."

2.8 It was further submitted that even if it is assessed as income from other sources, once this amount is made a part of book profit, remuneration to partners on this amount is allowable to assessee in view of decision of ITAT, Jaipur Bench in case of **S.P. Equipment & Services vs. ACIT (2010) 33 DTR 265**, where it was held that:

“ for the purpose of computing allowable deduction under s. 40(b), book profit has been defined under Explan. 3 thereto to mean the net profit as shown in the P&L a/c of the relevant previous year computed in the manner laid down in Chapter IV-D subject to specified adjustments. Selection of any head of income, more particularly “profit and gains of business or profession” is nowhere required or envisaged by the legislature. There is no substance in the contention of the Revenue that the receipts credited to P&L a/c should be assessed under different heads of income as classified under s.14. Legislature has not authorized exclusion of some receipts from P&L a/c even though they are non-business receipts. Explanation 3 nowhere empowers the AO to go behind the net profit shown in the P&L a/c except to the extent of adjustments provided therein. Since the book profit has been defined to be the net profit shown in the P&L a/c of the firm, it is the profit which the partners have agreed to share and, therefore such net profit has to be considered as business income at least for the purpose of s. 40(b). Provisions of s. 28(v) also support this view. If the nature of the income has been deemed by the legislature to be the business income by the recipient, the source also should bear the same character i.e. business income. Therefore, interest income is not to be excluded from the net profit declared by the assessee firm of computing book profit for the purpose of determining the allowable deduction of remuneration payable to the partners under s. 40(b). “

In any case, the AO himself has allowed remuneration to partners as claimed by the assessee which is after considering the excess stock surrendered by the assessee and therefore, this issue is not a matter of dispute by the Department before the Hon'ble ITAT. In view of the above addition confirmed by the Ld. CIT(A) be deleted.

2.9 The Id DR is heard who has relied on the orders of the lower authorities.

2.10 We have heard the rival contentions and pursued the material available on record. During the course of survey, the assessee has surrendered an amount of Rs. 70,04,814/- towards investment in stock of rice which had not been recorded in the books of accounts. Subsequently, in the books of accounts, the assessee has incorporated this transaction by debiting the purchase account and crediting the income from undisclosed sources. In the annual accounts, the purchases of Rs. 70,04,814/- were finally reflected as part of total purchases amounting to Rs. 33,47,19,658/- in the profit and loss account and the same also found included as part of the closing stock amounting to Rs. 1,94,42,569/- in the profit/loss account since the said stock of rice was not sold out. In addition to the purchases and the closing stock, the amount of Rs. 70,04,814 also found credited in the profit and loss account as income from undisclosed sources. The net effect of this double entry accounting treatment is that firstly the unrecorded stock of rice has been brought on the books and now forms part of the recorded stock which can be subsequently sold out and the profit/loss therefrom would be subject to tax as any other normal business transaction. Secondly, the unrecorded investment which has gone in purchase of such unrecorded stock of rice has been recorded in the books of accounts and offered to tax by crediting the said amount in the profit and loss account. Had this investment been made out of

known sources, there was no necessity for assessee to credit the profit/loss account and offer the same to tax. Accordingly, we donot see any infirmity in assessee's bringing such transaction in its books of accounts and the accounting treatment thereof so as to regularise its books of accounts. In fact, the same provides a credible base for Revenue to bring to tax subsequent profit/loss on sale of such stock of rice in future.

2.11 Having said that, the next issue that arises for consideration is whether the amount surrendered by way of investment in the unrecorded stock of rice has to be brought to tax under the head "business income" or "income from other sources". In the present case, the assessee is dealing in sale of foodgrains, rice and oil seeds, and the excess stock which has been found during the course of survey is stock of rice. Therefore, the investment in procurement of such stock of rice is clearly identifiable and related to the regular business stock of the assessee. The decision of the Co-ordinate Bench in case of Shri Ramnarayan Birla (supra) supports the case of the assessee in this regard. Therefore, the investment in the excess stock has to be brought to tax under the head "business income" and not under the head income from other sources". In the result, ground No.1 of the assessee is allowed.

3. In respect of Ground No. 2, the facts of the case are that the assessee has given loan and advances to Smt. Rita Gupta of Rs. 34,84,160/- and charged interest @ 10%, whereas assessee firm was paying interest @ 14%-17% on loans availed by it. The assessee was asked to explain as to why interest @ 14% is not charged from Smt. Rita Gupta as the assessee is paying such amount on loans availed by it. The assessee submitted that such interest is due to various reasons i.e. demand and supply of money, slack or boom season, period for which loans is given or taken etc. The assessee's contention was not accepted

by the AO. The AO observed that if the assessee had not advanced such loan to Smt. Rita Gupta, who is related to partners of assessee firm, then the amount would have been utilized to fund the firm and it would not have taken the loans where it is paying 14%-17% loans. Thus, this act was held prejudicial to the interest of the assessee firm and an amount of 4% (14%-10%) of the loan amount of Rs. 34,84,160/-, i.e. Rs. 1,39,366/- was added to the total income of the assessee and the matter was carried in appeal before the Id CIT(A).

3.1 The findings of the Id. CIT(A) is reproduced as under:

"I have gone through the assessment order as well as submissions made by the appellant and find that the AO has given cogent reason about charging of interest at 10% while paying interest rate of 14-17%. Accordingly, the disallowance of interest amounting to Rs. 1,39,366/- is sustained and the appellant's ground of appeal is dismissed."

3.2 The Id. AR of the assessee submitted that at the outset, it may be noted that the AO has made addition on account of notional interest of Rs. 1,39,366/-. There cannot be any addition on account of notional income as held by the Hon'ble Supreme Court in case of E.D.Sassoon & Co. & Ors. Vs. CIT (1954) 26 ITR 27 and Godhra Electricity Co. Ltd. vs. CIT (1997) 225 ITR 746 where it was held that only real income can be taxed, hypothetical income cannot be taxed nor income can be taxed in vacuum. Therefore, the addition made by the AO is not as per law and the same be deleted. The Id. CIT(A) has confirmed the addition by stating that it is the disallowance of interest. It is submitted that the lower authorities have not disputed about the commercial expediency about the advance given to Smt. Rita Gupta. In fact, the advance was given to Smt. Rita Gupta in earlier years for construction of godown and

the same was given on rent by the assessee. Therefore once commercial expediency for giving the advance is established, no part of the interest expenditure can be disallowed in view of the decision of Hon'ble Supreme Court in case of S.A. Builders 288 ITR 1 and Hero Cycles Pvt. Ltd. vs. CIT 379 ITR 347 where it was held that the Revenue cannot justifiably claim to put itself in the arm-chair of the businessman or in the position of the Board of Directors and assume the role to decide how much is reasonable expenditure having regard to the circumstances of the case. It further held that no businessman can be compelled to maximize his profit and that the income tax authorities must put themselves in the shoes of the assessee and see how a prudent businessman would act. The authorities must not look at the matter from their own viewpoint but that of a prudent businessman. Further, in past, no such disallowance/addition was made. Therefore, neither the addition of notional interest made by the AO or disallowance of interest as held by the Id. CIT(A) is as per law. It may also be noted that the partners of the firm have a capital of Rs. 1,96,73,637/-. Partners are paid interest @12%/ The balance in the partners account is much more than the amount advanced to Smt. Rita Gupta who is a wife of one of the partner. Therefore, even the disallowance made @4% is not justified and the same should be restricted @ 2% only. Reliance is also placed on the following cases:

- CIT vs. Ram Kishan Verma (2016) 132 DTR 107/132 Taxman 107 (Raj.) (HC)
- CIT vs. Vijay Solvex Ltd. (2015)113 DTR 382 (Raj.) (HC)

3.3. The Id DR is heard who has relied on the order of the lower authorities.

3.4 We have heard the rival contentions and perused the material available on record. It is noted that the advance was given to Smt. Rita Gupta in earlier years for construction of godown and the same was given on rent by the

assessee. The test of commercial expediency for giving the advance having being established, the AO is not correct to challenge the rate of interest which has been charged by the assessee. Further, no nexus has been established between the borrowed funds and funds advanced to Smt Rita Gupta. In the result, the ground no. 2 of the assessee is allowed.

In the result, the appeal filed by the assessee is allowed.

Order pronounced in the open court on 17/03/2017.

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

Sd/-
(VIKRAM SINGH YADAV)
लेखा सदस्य / Accountant Member

Jaipur

Dated:- 17/03/2017

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

1. अपीलार्थी / The Appellant- M/s Bajargan Traders, Alwar
2. प्रत्यर्थी / The Respondent- The ACIT, Circle-2, Alwar
3. आयकर आयुक्त / CIT Alwar
4. आयकर आयुक्त(अपील) / The CIT(A) Alwar
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, जयपुर / DR, ITAT, Jaipur
6. गार्ड फाईल / Guard File (ITA No. 137/JP/2017)

आदेशानुसार / By order,

सहायक पंजीकार / Assistant. Registrar.