

IN THE INCOME TAX APPELLATE TRIBUNAL  
"A" BENCH, MUMBAI

BEFORE SHRI S.RIFAUR RAHMAN (ACCOUNTANT MEMBER  
AND  
SHRI PAVAN KUMAR GADALE (JUDICIAL MEMBER)

I.T.A No. 3333/Mum/2019  
(Assessment year : 2014-15)

M/s Aricia Construction 1501, 15 <sup>th</sup> Floor, B-Wing 02 Commercial Complex, Opp. Asha Nagar, Mulund (W) Mumbai-400 080 PAN : AAOFA9504F	vs	ACIT -29(1), Mumbai
<b>APPELLANT</b>		<b>RESPONDENT</b>

Assessee represented by	Adv. Devendra Jain
Revenue represented by	Shri Mehul Jain (DR)

Date of hearing	25-10-2021
Date of pronouncement	03-01-2022

**ORDER**

**Per : S. Rifaur Rahman (AM):**

This is an appeal filed by the assessee against the order of the learned Commissioner of Income-tax (Appeals)-39, Mumbai for the assessment year 2014-15.

2. Assessee has filed following grounds of appeal, raising three grounds of appeal, they are-

- "1. The Learned CIT(A) has erred in by confirming disallowance of Rs. 10,41,3897- as excess interest paid to related persons specified u/s 40A(2)(b) of Income Tax Act, 1961.*
- 2. The Learned CIT(A) has erred in by confirming disallowance of Rs. 7,64,567 u/s 40(a)(ia) of income tax act, 1961 for non deduction of TDS on interest.*
- 3. The Learned CIT(A) has erred in disallowance of Rs.20,05,1997- being expenses accounted for on accrual basis under Site Expenses under the head Business Income."*

3. Brief facts relating to ground 1 are, during assessment proceedings the assessing officer observed that assessee had paid interest to two persons, i.e. Dura Tech and Hemali Gada @17% p.a. and 15% p.a., respectively. The assessing officer observed that the above two persons are specified persons as per section 40(A)(2)(b) of the Act and the interest paid to those persons were excessive. Accordingly, assessing officer restricted the interest payment @12% p.a. and made the disallowance of Rs.26,88,640/-.

4. Aggrieved, assessee preferred appeal before CIT(A) and before Ld.CIT(A) assessee filed the following submissions:-

*"The Appellant has debited Rs, 88,51,806/- & Rs. 4,25,833/- as interest paid to the loan party covered u/s 40A(2)(b) @ 17% & 15% respectively to the Profit & loss account for the year under consideration.*

*The Learned Assessing officer has disallowed the interest paid in excess of 12% u/s 40A(2)(b) stating that they are out of the ambit of scope of Section 37(1) of the Income Tax Act, 1961 since they are not incurred for wholly and exclusively for the business purpose.*

*Section 37(1) of the Income Tax Act, 1961 states that "Any expenditure (not being expenditure of the nature described in sections 30 to 36 and not being in the nature of capital expenditure or personal expenses of the assessee), laid out or expended wholly and exclusively for the purposes of the business or profession shall be allowed in computing the income chargeable under the head "Profits and Gains of Business or Profession". The funds so borrowed are used to make payment against purchases, BMC expenses, finance expenses, admin expenses, etc. Keeping in mind the nature of business of appellant, it can be seen that the funds have been borrowed and utilized wholly and exclusively for the purpose of business. Therefore, it fulfills the criteria of allowability of*

expenses as business expenditure as per section 37(1) of the Income Tax Act, 1961.

*In response to the above, we would like to state that nowhere in the section 40A(2) the rate of interest is specified as 12% nor the rate higher than 12% is mentioned excessive or unreasonable. Thus the rate of interest of 17% & 15% cannot be said to be unreasonable or excessive keeping in view the market rate and other factors.*

*The funds has been borrowed taking into account many factors such as "Business requirements, safety factors, urgency of funds, receipt of funds at a short notice and repayment at any time facility given, repayment of any amount i.e. no fixed amount, no mortgage or security i.e. totally unsecured. Market Creditability also does not get affected if funds are borrowed from the sister concern. "*

.....

*Further the nature of business being construction activity; it is very difficult to raise funds from the market. Also the funds at a rate of 15% or 18% have been borrowed from the parties which are not related as per section 40A(2)(b) of the Income Tax Act.*

.....

*Based on the above fact reliance can be placed on the following case laws for explaining that it is on part of businessman to determine which expenses are necessary for conducting his business activities –*

1. *"When there is nexus between the expenditure incurred and purpose of business, the Assessing Officer cannot substitute his opinion about the reasonableness or not of the expenditure as if the Assessing Officer was the businessman," CIT v, Devaghi Beverages Ltd. (2007) 197 Taxation 444 (Del) (High Court)*

2. *"Once it is found that there was a nexus between the expenditure incurred by the assessee and his business and genuineness of the expenditure incurred by the assessee and his business and genuineness of the business was not disputed, the Assessing Officer could not sit in the arm chair of the businessman to determine as to what amount of the expenses he ought to incur for doing his business." CIT v. Padmini Packaging P. Ltd (2006) 193 Taxation 558 (Bom.) (High Court)*

3. *"Whenever a claim is made by the assessee before the Income Tax Officer for allowing an expenditure as a legitimate business expenditure, ITO must try to put himself in shoes of a prudent businessman and try to look at the matter from that point of view. A businessman may make an expenditure which he is under no legal obligation to make, but if he does so as a measure of commercial expediency it must be allowed under section 37 as legitimate business expenditure. (A, Y. 1978-79) " Abbas Wazir P. Ltd v, CIT (2003) 133 Taxman 702/185 CTR152 / (2004) 265ITR 77 (AIL) (High Court)*

*Based on the above facts, we pray your honor to delete the disallowance of the interest paid to persons specified u/s 40A(2)(b) in excess of 12% amounting to Rs.26,88,640/-."*

5. After considering the detailed submissions of the assessee, the Ld.CIT(A) observed that the assessee's contention has merit and the unsecured loans carry higher risk for the lenders and therefore, rate of interest charged is higher than the rate of interest charged on secured loans. Accordingly, held that the rate of interest @15% would be reasonable. Accordingly, he allowed the interest payment to Hemali Gada whereas with regard to interest payment to Dura Tech, he held that rate of interest @15% p.a. is reasonable and accordingly, he disallowed 2% excessive payment to Dura Tech. Accordingly, he partly allowed the ground raised by the assessee.

6. Aggrieved, assessee is in appeal before us.

7. The learned AR brought to our notice the above facts on record and submitted that Ld.CIT(A) has not given any finding and he brought to our notice page 41 of the paper book to submit that assessee has paid interest to non specified parties during assessment year 2014-15 carrying interest @18%. He submitted that the assessee has paid interest @18% to non specified persons, therefore, the payment of interest @17% to Dura Tech is reasonable. For this purpose, he relied upon the case law in CIT vs Dempo & Co Pvt Ltd (2011) 196 Taxman 193 (Bom).

8. On the other hand, the learned Departmental Representative relied on the order passed by the Ld.CIT(A) and he also brought to our notice pages 41 & 42 of the paper book filed by the assessee to highlight that assessee has paid interest at less than 18% whereas to specified persons assessee has paid between 11.7% to 17% to other non specified persons. Therefore, he submitted that the findings of Ld.CIT(A) is reasonable.

9. Considered the rival submissions and material placed on record. We observe from the record that assessee has paid interest to several parties and paid interest between 11.5% to 18% during this assessment year and assessee has taken loans from specified persons, viz. Dura Tech and Hemali Gada and paid interest to them @15% to 17%, respectively. Since the unsecured loan availed by the assessee from several parties, and agree that the risk to non specified persons is more than the specified persons and Ld.CIT(A) has pegged the rate @15% whereas assessing officer restricted it at 12%. Considering the information available on record, in our considered view, Ld.CIT(A) has pegged @15% which is reasonable when compared to the average rate of unsecured loan for the whole assessment year, it will be more or less 15%. Therefore, we do not see any reason to disturb the findings of Ld.CIT(A). Accordingly, ground raised by the assessee is dismissed.

10. With regard to ground 2, the relevant facts are during assessment proceedings, assessing officer observed that assessee did not deduct tax at source in respect of interest payment of Rs.7,64,567/-. The assessee submitted that the tax was not deducted at source because parties had stated that their income was below the taxable limit. The assessing officer rejected the contentions of the assessee and observed that assessee has not filed form 15G / 15H from those parties, who stated that their income is less than taxable limit. When enquired, assessee filed details before the assessing officer and assessing officer observed that assessee has not filed party-wise details and amount of interest. Since assessee has not complied with the above conditions, he disallowed the amount of Rs.7,64,567/- under section 40(a)(ia) of the Act. Aggrieved, assessee preferred appeal before CIT(A) and before CIT(A), assessee filed form 15G / 15H in respect

of six recipients of interest. After considering the submissions of the assessee, Ld.CIT(A) observed that assessee submitted copies of form 15G / 15H which were submitted by the persons to whom the interest was paid. He observed that on going through those forms, he found that forms were defective inasmuch as many of the columns were not filled up. He, therefore, held that the case of the recipients of the interest were not covered by section 197A of the Act. Accordingly, he sustained the addition made by the assessing officer. Aggrieved, assessee is in appeal before us.

11. At the time of hearing, learned AR brought to our notice form 15G / 15H filed by recipients of interest which are placed at pages 43 to 45 of the paper book and prayed that addition may be deleted.

12. On the other hand, learned DR relied on the findings of Ld.CIT(A).

13. Considered the rival submissions and perused the materials placed on record. We observe from the record and submissions made by Ld.AR and have gone through the forms which were filed by the recipients of interest which shows that these forms were filed specifically for assessment year 2014-15. The informations submitted before us indicate all the relevant informations required to make the claim of interest without deducting tax at source. We do not see any reason to reject of the claim of the assessee. Therefore, we direct the assessing officer to allow the claim of the assessee to the extent the amounts are mentioned in the above said form 15G / 15H. Accordingly ground raised by the assessee is allowed.

14. With regard to ground 3, during assessment proceedings assessee was asked for details of expenditure incurred of Rs.5,17,43,610/- towards purchase,

labour and site expenses alongwith supporting evidences. In response, assessee submitted the details of expenditure party-wise / head-wise for Rs.3,12,50,618/- alongwith sample invoices. The assessing officer gave further opportunity for filing entire details of expenses. Since no co-operation from the assessee, the assessing officer proceeded to disallow 25% of the differential expenditure of Rs.2,04,92,992/- (Rs.5,17,43,610/- (-) Rs.3,12,50,618/-). Aggrieved, assessee preferred appeal before learned CIT(A) and made the following submissions:-

*"The Appellant has incurred the Rs, 11,32,60,827/- as the project cost under the Dalai Cottage Project. Out of which Rs. 5,17,43,610/- is expenses incurred towards Purchase, Labour & Site Expenses from the beginning of the project. The Appellant has debited Rs. 3,12,50,61s/- as purchases to the Profit & loss account for the year under consideration. The details and evidence for the verification of the same is submitted vide Pt.4 of letter dated 26/12/2016. Out of balance expenses, major expenses are pertains to the earlier years. The same were also subject to scrutiny. The Assessment Orders for A. Y, 2012-13 & A.Y. 2013-14 is enclosed herewith. Enclosing herewith the relevant Audited Profit & Loss Account highlighting the purchases of Rs. 3,12,50,618 included during the year for your reference.*

*The Learned Assessing officer has added back the 25% of differential expenditure of Rs, 2,04,92,992/- (Rs. 5,17,43,610 - Rs. 3,12,50,618) stating they are unverifiable expenses.*

*Expenses have been incurred exclusively and directly for the Appellant's business. The above expense is the normal business expenditure Incurred in the course of running the business. No particular expenses has been pointed out which does not relate to the business of the appellant, Merely expenses are not verifiable cannot be a ground for disallowance or additions.*

***Further it was held by Hon'ble Supreme Court in the case of CIT Vs. DhanrajgiriNarain Singh Girji 91 ITR 544 that it is not open to the department to prescribe what expenditure an assessee should incur and in what circumstances he should incur that expenditure. Every businessman knows his interest best***

*Ad hoc addition without pointing out nature of discrepancies is not proper. The addition made by Learned Assessing officer has been made in a most arbitrary and casual manner without any basis.*

*Therefore, any addition on the ground of unverifiable expenses does not seem to be appropriate and hence the ad-hoc disallowance in this case needs to be deleted."*

15. After considering the submissions of the assessee, learned CIT(A) observed that assessing officer has not pointed out any specific instance where supporting evidences were not available and he also observed that assessing officer made

the disallowance of expenses in an arbitrary manner. Ld.CIT(A) gave partial relief to the assessee with the following observations:-

*"7.4.3 The appellant submitted that site expenses it had incurred more site expenses of Rs. 54,22,325A during the year for which bills were raised by the seller in the P.Y. 2014-15. The AR contended that the AO allowed the site expenses and purchases of Rs. 3,12,50,618 relating to the P.Y. 2013-14 in full but wrongly disallowed 25% of the remaining site expenses and purchases which comprised of those relating to P.Y. 2010-11, P.Y. 2011-12, P.Y. 2012-13 and the sum of Rs, 54,22,325/- during the year for which bills were raised by the seller in the P.Y. 2014-15.*

*7.4.4 The AR also filed a statement showing details of site expenses for the project Dalai Cottage. Regarding the site expenses of Rs.54,22,325/-, the AR submitted that bills were raised during the F.Y. 2014-15. The AR submitted that the expenses were accounted for in the F.Y, 2013-14 and were not claimed in F.Y. 2014-15.*

*7.4.5 It is seen that expenditure towards site expenses debited to the P&L Account was Rs.54,22,325/-. The expenditure disallowed by AO was Rs.51,23,248/-. I propose to disallow the expenses debited to the P&L Account of Rs.54,22,325/- since they do not pertain to F.Y. 2013-14. This will result in enhancement in part. In the course of the appellate proceedings, the AR was requested to file his objections, if any, by 22.01.2019.*

*7.4.6 In response the AR submitted, without prejudice to his claim that the provision for site expenses were allowable, that the provision for site expenses were taken into consideration of Total Project Cost and consequently in computation of closing stock. He submitted that in case the provision for site expenses are disallowed, the closing stock should be recomputed.*

*7.4.7 After considering all the facts, I hold that the expenditure of Rs.54,22,325/- for which bills were raised in the subsequent year are not allowable. However, I accept the appellant's contention that the closing stock needs to be recomputed in view of the disallowance of site expenses because part of those expenses forms part of the closing stock. The value of the closing stock (unsold area of 7,696 sq, ft,) is reworked below in view of the disallowance of site expenses of Rs, 54,22,325/-."*

16. At the time of hearing, learned AR brought to our notice the facts on record. He brought to our notice the submissions made before learned CIT(A) which is placed on record at page 56 of the paper book. He brought to our notice pages 61 to 64 of the paper book and other bills filed in the paper book. He prayed that the expenses incurred for the purpose of business and the purchases which includes site expenses are part of total project cost and will be included in

the valuation of closing stock. He further submitted that tax authorities cannot make adhoc disallowance and prayed that the disallowance may be deleted.

17. On the other hand, learned DR relied on the findings of learned CIT(A).

18. Considered rival submissions, perused material placed on record. We observe from the record that assessee is in the construction business and the cost involved are relating to purchase of raw materials, site development and other construction expenses. It is a fact on record that there might be certain expenses in relation to site development for which assessee may have to generate self made vouchers. The cost incurred relating to site development as well as cost of construction will be part of closing stock. We observe that assessing officer has called for details of the expenses alongwith invoices. Assessee has filed details of expenditure to the extent of Rs.3,12,50,618/- with sample invoices. Assessing officer has accepted those expenditure after verifying sample invoices. However, we observe from the findings of learned CIT(A) that he has considered the year-wise expenditure submitted by the assessee to the extent of Rs.4,63,21,285/- incurred by the assessee from previous years 2010-11 to 2013-14. He also observed that assessee also incurred site expenses of Rs.54,23,225/- during the year for which bills were raised by the parties in 2014-15 (A.Y. 2015-16). He also observed from the submissions of the assessee that assessing officer allowed the site expenses and purchases of Rs.3,12,56,618/- relating to previous year 2013-14 in full, but wrongly disallowed 25% of the remaining site expenses and purchases, which comprised of those related to previous years 2010-11 to 2012-13. He acknowledged the submissions of the assessee that site expenses of Rs.54,22,325/- which is relating to financial year 2014-15 relevant to assessment

year 2015-16. Accordingly, he proceeded to sustain the disallowance to that extent. At the same time, he gave a reduction of Rs.34,17,176/- relating to the reduction in the valuation of closing stock to the extent of 7695 sq.ft. of unsold area. After careful consideration, we observe that assessee has claimed the expenditure in the year of actual addition to the cost of the project. However, the bills were raised in the next assessment year i.e. in F.Y. 2014-15 (AY 2015-16). As a prudent method of accounting adopts the income and expenditure on matching principle. The cost is incurred but the actual bills were raised in the subsequent year. It does not change the character of the expenditure but only timing to record the bills. In actual, all the costs incurred are charged to work-in-progress. It does not make any difference when actual bills are recorded. The important thing is whether the cost is incurred for the project. Therefore, in our considered view, the addition sustained by the learned CIT(A) is not proper and accordingly, the ground raised by the assessee is allowed.

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

Order pronounced on 03/01/2022.

Sd/-

sd/-

<b>(PAVAN KUMAR GADALE)</b>	<b>(S. RIFAUR RAHMAN)</b>
<b>JUDICIAL MEMBER</b>	<b>ACCOUNTANT MEMBER</b>

Mumbai, Dt : 03/01/2022

Pavanan

Copy to :

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  2. Respondent
  3. The CIT concerned
  4. The CIT(A)
  5. The DR, ITAT, Mumbai
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By Order

Asstt. Registrar, ITAT, Mumbai