

IN THE INCOME TAX APPELLATE TRIBUNAL
RAJKOT BENCH, RAJKOT

[CONDUCTED THROUGH VIRTUAL COURT]

**Before: Shri Waseem Ahmed, Accountant Member
And Shri Siddhartha Nautiyal, Judicial Member**

**ITA No. 06 /Rjt/2018
Assessment Year 2014-15**

M/s. Shivabyay Project Pvt. Limited, Plot No. 305, Ward- 12B, Komal Complex, Office No. 14 & 6, Gandhidham-370201 PAN: AAJCA3934D (Appellant)	Vs	The ITO, Ward-2, Gandhidham (Respondent)
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**ITA No. 37/Rjt/2018
Assessment Year 2014-15**

The ITO, Ward-2, Gandhidham (Appellant)	Vs	M/s. Shivabyay Project Pvt. Limited, Plot No. 305, Ward- 12B, Komal Complex, Office No. 14 & 6, Gandhidham-370201 PAN: AAJCA3934D (Respondent)
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**Assessee by: Written Submission
Revenue by: Shri K.L. Solanki, Sr. D.R.**

Date of hearing : 02-11-2023
Date of pronouncement : 08-11-2023

आदेश/ORDER

PER : SIDDHARTHA NAUTIYAL, JUDICIAL MEMBER:-

These are cross appeals filed by the Department and assessee for A.Y. 2014-15, arise from order of the CIT(A)-2, Rajkot dated 24-11-2017, in proceedings under section 144 of the Income Tax Act, 1961; in short “the Act”.

2. The assessee has taken the following grounds of appeal:

“The grounds of appeal mentioned herein under are without prejudice to each other.

1.0 Ld. Commissioner of Income tax (Appeals)-1, Rajkot has erred in law in confirming the disallowance of Rs, 13,32,500/- u/s 40(a)(ia) of the Income Tax Act,1961 in relation to following expenses, which may kindly be allowed and justice be done;

<i>Description</i>	<i>Amount</i>
<i>Account writing charges</i>	<i>85,500</i>
<i>Commission expenses</i>	<i>3,00,000</i>
<i>Legal & professional fees</i>	<i>5,84,000</i>
<i>Rent expenses</i>	<i>3,63,000</i>
<i>Total</i>	<i>13,32,500/-</i>

2.0 Ld. Commissioner of Income tax (Appeals)-2, Rajkot has erred in law in confirming the disallowance of Rs. 13,32,500/- u/s 40(a)(ia) of the Income Tax Act,1961, despite the fact that the book result was rejected u/s 145(3) of the Income-tax Act, 1961, which may kindly be allowed and justice be done;

Your appellant craves leave to add, alter or withdraw any one or more grounds of appeal;

3. The Revenue has taken the following grounds of appeal:

“1. The Ld. CIT (A) has erred in deleting the addition of Rs. 1,82,60,293/- out of total addition of Rs. 1,95,92,793/- made on account of disallowance of expenses claimed u/s 40(a)(ia) of the I.T. Act.

2. It is therefore prayed that the addition of Rs. 1,95,92,793/- on account of disallowance of expenses claimed u/s 40(a)(ia) of the Act as held in the assessment order be restored.”

4. The brief facts of the case are that for the impugned year under consideration, the assessee had disclosed gross profit of Rs. 74,00,274/- on turnover of Rs. 6,40,83,340/-. During the course of assessment, despite several opportunities, the Assessing Officer observed that the assessee did not produce records/books/details/supporting documents to justify the profit declared by the assessee. Accordingly, the Assessing Officer rejected the books of accounts of the assessee and adopted the ratio of gross profit @ 14.59%, which was the same GP ratio as in the immediately preceding assessment year 2013-14. Accordingly, by applying the aforesaid GP ratio of 14.59%, the turnover of the assessee was worked out at Rs. 93,49,759/- as against the profit of Rs. 74,00,274/- disclosed by the assessee. Accordingly, the Assessing Officer added the difference of Rs. 19,49,485/- to the total income of the assessee. After having rejected the books of accounts, the Assessing Officer observed that the assessee had claimed expenses amounting to Rs. 1,95,92,793/- on which TDS was not deducted by the assessee. Accordingly, the Assessing Officer held that since assessee did not

file any submission with regard to non-deduction of tax at source on the aforesaid payments, the Assessing Officer disallowed the expenses amounting to Rs. 1,95,92,793/- u/s. 40(a)(ia) of the Act and added to the total income of the assessee.

5. In appeal, the assessee did not challenge the ground relating to rejection of the books of the accounts. However, the assessee submitted that once the books of accounts have been rejected and the profit of the assessee has been calculated on an estimation basis then it is a well established law no further disallowance can be made u/s. 40(a)(ia) of the Act. In light of submissions made by the assessee, the Id. CIT(A) held that expenses which have become part of estimation on gross profits cannot be subjected to disallowance u/s 40(a)(ia) of the Act. Accordingly, the Id. CIT(A) deleted the disallowance amounting to Rs. 1,82,60,293/- which was added by the Assessing Officer u/s. 40(a)(ia) of the Act. However, the Id. CIT(A) sustained the disallowance u/s. 40(a)(ia) of the Act amounting to Rs. 13,32,500/- on the ground that these expenses do not fall in the estimation of gross profit and therefore, they are liable to be disallowed u/s. 40(a)(ia) of the Act while passing the order of Id. CIT(A) made the following observations:-

“4.2.3 Decision

During appellate proceedings the assessee has contested this disallowance placing reliance inter alia upon the decision of Honourable ITAT bench Rajkot in case ACIT VS OMKAR hadipur 20/01/2012 in ITA No. 998/Rjt/2010 where in it has been held that when profit rate has been estimated after rejection of books of accounts u/s 145(3) the provision of section 40(a)(ia) will not be applicable. The relevant portion of the decision of ITAT is reproduced below.

"Para-9: In respect of controversy involved in ground No. (b), we have heard both sides. The only grievance of revenue is that by rejecting the books of account u/s 145(3), the A.O. made addition of Rs. 46,42,313/-. This has been reduced by Id. CIT(A) to 8,80,827/-. The reasoning given Id. CIT(A) for deleting the entire addition of Rs. 1,00,03,012/- which was made by AO u/s 40(a)(ia) is that once income is determined by applying flat net profit rate, the provisions of sec. 40(a)(ia) will not be applicable. He submitted that large addition made cannot include small addition. Therefore, at the most, the benefit only to the extent of Rs. 8,80,827/- can be given out of addition of Rs. 1,00,03,012/-. As against this the counsel of the assessee pointed out that in the judgement of Hon'ble Allahabad High Court in the case of CIT vs. Banwarilal Banshidhar 229 ITR 229 held that where income is computed by applying gross profit rate, separate addition u/s 40A(3) cannot be made. Similar view is also taken by Andhra Pradesh High Court in the case of Indwell Constructions vs. CIT (1998) 232 ITR 776 and ITAT Ahmedabad Bench in the case of New Narayan Builders vs ITO (1992) 43 TTJ 508. It is pertinent to note that in the impugned order, Id. CIT(A) has followed the aforesaid three decisions. We therefore, inclined to uphold the order of Id. CIT(A)."

Respectfully following the above binding decision of Honourable Jurisdictional HAT, I am of the considered opinion that the expenses which have become part of estimation of G.P. should not be subjected to disallowances u/s 40(a)(ia). However, I find that in the total disallowance of Rs 1,95,92,393/- the following expenses do not fall in the estimated G.P.

Branch	Description	Amount
Administrative exp	Account writing charges	85500
Do	Commission expenses	300000
Do	Legal & Professional fees	584000
Do	Rent expenses	363000
	Total	1332500

The assessee has not contended that any TDS was made in respect of these expenses or on merit they do not warrant disallowance u/s 40(a)(ia). Accordingly an addition of Rs 13,32,500/- is sustained and balance addition of Rs 1,82,60,293/- is deleted. Assessee succeeds partly on this ground."

6. Both the Department and the assessee are in appeal before us against the aforesaid order passed by Id. CIT(A)

7. We shall first take up the Department's appeal.

8. The Department's contentions is that Id. CIT(A) has erred in deleting addition of Rs. 1,82,60,293/- out of total addition of Rs. 1,95,92,793/- made on account of disallowance of expenses claimed u/s. 40(a)(ia) of the Act. On going through the facts of the assessee's case and judicial precedents on the subject, it is a well settled law that once income has been computed by applying the gross profit ratio, separate addition u/s. 40(a)(ia) cannot be made. In the case of **Power Liners Vs. ACIT (ITAT Jaipur) ITA No. 194/JP/2017**, the ITAT held that no disallowance can be made u/s. 40(a)(ia) where net profit have been estimated. The ITAT held that once the income of the assessee was estimated after rejection of books of account, then the AO could not make disallowance on the same books of account for the purpose of disallowance by invoking provisions of section 40(a)(ia) or general disallowance under section 37(1) of Income Tax Act, 1961. In the case of **J.S. Grover Constructions 82 taxmann.com 117 (Amritsar - Trib.)**, the ITAT held that once books of account are rejected and income is estimated by applying net profit rate, no further disallowance can be made under section 40(a)(ia). In the case of **Lali Construction Co. 54 taxmann.com 68 (Punjab & Haryana)**, the High Court held that deduction of interest paid on borrowed capital is not allowable where income is estimated by applying net profit rate. In the case of **Indwell Constructions 232 ITR 776 (Andhra Pradesh)**, the High Court held that

where books of account of assessee-firm, which was doing contract business, were rejected and its income was estimated by applying proviso to section 145, no separate addition on account of interest and salary paid to partners could be made to such estimated income by Commissioner under section 263. In the case of **Banwari Lal Banshidhar 229 ITR 229 (All.)** where income of assessee was computed applying gross profit rate and when no deduction was claimed or allowed to assessee in respect of purchases, no disallowance under section 40A(3), read with rule 6DD(j), could be made by Assessing Officer. Further in the decision of Jurisdictional High Court of Gujarat in the case of **CIT(A) vs. Dhiraj Rungat 20199 Tax PUB (DT 3786 (Gujarat High Court))** has held that where the books of accounts were rejected by the Assessing Officer further additions could not be made by the Department relying upon the same books of accounts. Further, the ITAT Rajkot in the case of ACIT vs. M/s. Omkar Engineering Company in ITA No. 998/Rjt/2010 has made the following observation in this regard:-

“9. In respect of controversy involved in ground No.(b), we have heard both sides. The only grievance of revenue is that by rejecting the books of account u/s. 145(3), the AO made addition of Rs.46,42,313/-. This has been reduced by ld. CIT(A) to Rs.8,80,827/-. The reasoning given by ld. CIT(A) for deleting the entire addition of Rs.1,00,03,012/- which was made by AO u/s 40(a)(ia) is that once income is determined by applying flat net profit rate, the provision of sec.40(a)(ia) will not be applicable. He submitted that large addition made cannot include small addition. Therefore, at the most, the benefit only to the extent of Rs.8,80,827/- can be given out of addition of Rs.1,00,03,012/-. As against this, the counsel of the assessee pointed out that in the judgment of Hon'ble Allahabad High Court in the case of CIT vs. Banwarilal Banshidhar 229 ITR 229 held that where income is computed by applying gross profit rate, separate addition u/s.40A(3) cannot be made. Similar view is also taken by Andhra Pradesh High Court in the case of Indwell Constructions vs. CIT (1998) 232 ITR 776 and 7 ITAT Ahmedabad Bench in the case of New Narayan Builders

vs. ITO (1992) 43 TTJ 508. It is pertinent to note that in the impugned order, ld. CIT(A) has followed the aforesaid three decisions. We therefore, incline to uphold the order of ld. CIT(A)."

8. Accordingly, in light of the judicial precedent highlighted above including the once rendered by the Jurisdictional Gujarat High Court and also the ITAT Rajkot Bench, we are of the considered view that once the Assessing Officer has estimated the gross profit after rejecting the books of accounts of the assessee and the gross profit ratio has been arrived at on an estimation basis, there is no further scope of disallowance u/s. 40(a)(ia) of the Act. Accordingly, in light of above discussion and judicial precedent on the subject, the Department's appeal is hereby dismissed.

9. Now, we shall discuss the assessee's appeal

10. The assessee is in appeal against the confirmation of disallowance u/s. 40(a)(ia) of the Act in respect of certain expenses amounting to Rs. 13,32,500/-. The contention of the ld. counsel for the assessee is that once the books of accounts have been rejected u/s. 145(3) of the Act, then no further disallowance can be called for u/s. 40(a)(ia) of the Act.

11. We observe that while confirming the aforesaid disallowance, the ld. CIT(A) has stated that the aforesaid expenses do not fall in the estimation of GP ratio. While holding so, the ld. CIT(A) has not given any reasoning or rational as to why and on what basis it can be concluded that these expenses do not fall in the estimation of GP ratio. As observed by us in the preceding paragraphs, once the books of accounts have been rejected and the gross

profits have been calculated by the Assessing Officer on a estimation basis, there is no scope of invocation of section 40(a)(ia) of the Act for making further disallowance. In light of above observations and the judicial precedents on the subject, the appeal of the assessee succeeds.

12. In the result, the appeal of the assessee is allowed.
13. In the combined result, the appeal of the Department is dismissed and the appeal of the assessee is allowed.

Order pronounced in the open court on 08-11-2023

Sd/-
(WASEEM AHMED)
ACCOUNTANT MEMBER
Ahmedabad : Dated 08/11/2023

Sd/-
(SIDDHARTHA NAUTIYAL)
JUDICIAL MEMBER

आदेश की प्रतिलिपि अग्रेषित / Copy of Order Forwarded to:-

1. Assessee
2. Revenue
3. Concerned CIT
4. CIT (A)
5. DR, ITAT, Ahmedabad
6. Guard file.

By order,

Assistant Registrar,
Income Tax Appellate Tribunal,
Rajkot