

**IN THE INCOME TAX APPELLATE TRIBUNAL
“B” BENCH: BANGALORE**

**BEFORE SHRI CHANDRA POOJARI, ACCOUNTANT MEMBER
AND
SMT. BEENA PILLAI, JUDICIAL MEMBER**

ITA No.1005/Bang/2023
Assessment Year: 2015-16

Primavera Projects-N-Constructions Limited 226,3 rd Floor, 311/4, Ranka Chambers Cunningham Road Bengaluru 560 052. PAN NO : AADCP5738J	Vs.	DCIT Circle-5(1)(2) Bangalore
APPELLANT		RESPONDENT

Appellant by	:	Ms. Suman Lunkar, A.R.
Respondent by	:	Sri Subramanian S., D.R.

Date of Hearing	:	08.07.2024
Date of Pronouncement	:	08.07.2024

O R D E R

PER CHANDRA POOJARI, ACCOUNTANT MEMBER:

This appeal by assessee is directed against order of NFAC for the assessment year 2015-16 passed u/s 250 of the Income Tax Act, 1961 (in short “the Act”). The assessee raised following grounds:

1. *“The learned Commissioner of Income Tax (Appeals), NFAC, Delhi has erred in confirming the assessment order passed by the Assessing officer. The order passed by CIT(A), confirming the assessment order being bad in law is required to be quashed.*
- 2.1 *In any case, the Learned CIT(A) has erred in confirming the disallowance made by the Assessing officer amounting to Rs. 96,90,000/- u/s 37(1) of the Act by treating the sub contracting entities as Shell companies and holding that they did not do any work. On proper appreciation of facts and the law applicable, the sub contract expenses incurred for carrying on the business and therefore the provisions of section 37(1) are not applicable to the facts of the case. The conclusion drawn as being wholly erroneous both on facts and law is to be disregarded.*

2.2 *The authorities below have erred in not appreciating the fact that*

- i) *the sub contract expenditure debited were legitimate business expenses incurred for completion of the projects*
- ii) *The payments were made. through banking channel after deducting tax at source.*

The lower authorities have erred in disallowing the expenditure debited on the ground that the sub-contractors were shell entities. The action of authorities below being contrary to facts and law applicable is to be negated and the disallowance of expenses as made is to be deleted.

2.3 *In any case, the disallowance as made and confirmed is erroneous—and excessive.*

3.1 *The learned CIT(A) has also erred in confirming the addition made by the Assessing officer by treating the balances due to two sub-contractors as cessation of trading liability on the ground that subcontractors were shell entities. The conclusion drawn is wholly erroneous both on facts and law applicable and is to be rejected and the addition made is to be deleted.*

3.2 *In any case, the action of Assessing Officer, in making the addition in the last para of the order, on the basis of cessation of liabilities, makes it clear that liability did exist and was genuine and therefore on this ground also the addition as made becomes erroneous and is to be deleted.*

3.3 *In any case and without prejudice, the outstanding balance having arisen from the transaction for which there was debit to profit and loss account and which has been disallowed, the addition of outstanding balance amount to double addition and therefore has to be deleted.*

4. *In any case, the Assessing Officer has erred in holding the issue against the appellant on the grounds that:*

- a) *the sub-contractors were shell entities;*
- b) *the Sub contractor entities were deregistered under VAT Act, 2005;*
- c) *the sub-contractors had not filed the VAT returns;*

These conclusions are without basis and not in accordance with actual facts of the case, The appellant had actually given sub-contract and therefore these conclusions are to be ignored and sub-contract expenses are to be allowed as deduction;

5. *The appellant denies the liability pay interest u/s 234B of the Act. The interest having been levied erroneously is to be deleted.*

6. *In view of the above and on other grounds to be adduced at the time of hearing, it is requested that the impugned orders to the extent confirmed be quashed or at least the disallowances as made and confirmed be deleted and interest levied be also deleted.”*

2. Ground No.1 is general in nature, which do not require any adjudication.

3. Ground Nos.2.1 to 2.3 are with regard to disallowance of Rs.96.90 lakhs u/s 37(1) of the Act. Treating the sub-contracts as bogus payment.

4. Facts of the case and the submission of the ld. A.R. are as follows:

(i) S.K. Infrastructures Payment made Rs. 71,40,000/- and Trade Payables Rs.54,11,497/-:-

4.1 The assessee entered into contract with BWSSB (a Government of Karnataka body) to execute three Ground Level Reservoirs in different locations. The assessee entered into a subcontract agreement with S K Infrastructures to execute the work. A copy of the Memorandum of Understanding entered with the subcontractor was filed before the AO. AO in his order in para 4 stated that "However, the assessee did not produce any bills, instead only a "Contract Certificate" was produced by the assessee. It was seen that the same is between the assessee and the client BWSSB and there were no mention of the subcontract". According to assessee, as per the subcontract agreement the subcontractor cannot deal with the client directly as they have no business relationship with the client. They also should not reveal their identity. All the correspondence and other billing process has to be routed through the assessee. The payment shall also be received by the client against the work completed. Consequently, the measurements for work completion has to be made by the subcontractor to the client on behalf of the assessee. Based on this Work completion certificate and Progress Bill submitted to the client, the client would release the money to the assessee. Under these

circumstances, the subcontractor making a bill does not arise. They will be paid based on the Contract Certificate. Based on the MOU entered with the subcontractor the assessee would release funds to the subcontractor by making appropriate TDS deduction. It is pertinent to note here that the AO has not raised any doubts on the work executed, his reservation is only for making payment to a subcontractor without a bill. This shows that the assessee has incurred such expenditure to execute the contract through a subcontractor instead of executing by themselves directly by using direct labour.

4.2 The Id. A.R. for the assessee submitted that the assessee was due to pay, based on the Contract Certificate Rs.70,00,000/- on 23-06-2014 to S K Infrastructure. They should have deducted 2% TDS on this amount and remitted Rs.68,60,000/-. They made as mistake of not deducting TDS and hence they paid Rs.70,00,000/- in full. Subsequently they realized their mistake and remitted Rs.1,40,000/- TDS and debited to the S K Infrastructure account on 30-06-2014. The books of accounts were showing Trade Payables against S K Infrastructure for the work completed by them earlier and payments not made. The balance payable as 31-03-2015 is Rs.54,11,497/-. The AO has disallowed Rs. 71,40,000/- being payment made to subcontractor inclusive of TDS remittance and added back Rs. 54,11,497/- being the Trade Payables. It is general practice in the Construction business for Contractors to sub contract the work they are to execute for cost control and better margins of profit. For the same reason the assessee has given this contract on sub contract. The subcontractors are independent entities who are no way connected to the assessee. They are responsible for their business and assessee cannot be held responsible for their noncompliance of legal responsibilities. Mere fact that the sub-contractor fails to file his VAT return or that he has de-registered himself for VAT subsequent to the date of execution of contract does not amount to 'Shell Entity'.

S K Infrastructure has surrendered their VAT registration in FY 2016-17 (December 2016) which is much later to the date of payments made by the assessee. The onus of legal compliance is with the subcontractor and not with the assessee. The reasons given by AO has no basis nor any reliance to prove that the assessee has dealt with 'Shell Entities'.

4.3 The assessee has executed the same job in the earlier years also with the same subcontractors and during the assessment proceedings then, such questions have not been raised and they have accepted the validity of subcontract. It is beyond doubt that the assessee has incurred such expenditure to execute the contract. She submitted that it is also very important to note that the assessee has dealt with Government departments and not with any private parties. The department has approved the work completed by issuing 'Contract Certificate'. Hence the disallowance of Rs.71,40,000/- and add back of Creditors Rs. 54,11,497/- with regard to S K Infrastructures is unjustified and the same may be set aside.

(ii). Matha Infratech Private Limited Payment made Rs.25,50,000/- and Trade Payables Rs.9,36,597/-

4.4 The assessee entered into contract with RITES (Government of India Enterprise) to execute construction of Government Polytechnic College at Turuvekere. They entered into a subcontract agreement with Matha Infratech Private Limited to execute the work. A copy of the Sub contract Agreement entered with the subcontractor dated 28th June 2010 was filed before the AO. As per the agreement Matha Infratech is to carry out the contract work and the assessee to retain 5% as their commission on the gross bill before they release the payment to Matha Infratech. Matha Infratech was responsible to execute the work and get it certified by the client. As referred in the case of S K Infrastructure in the above paragraphs, in this case also the subcontractor was paid against the billing done to the client and appropriate TDS is made against all the payments.

4.5 The ld. A.R. submitted that during the FY 2014-15 relevant to assessment year 2015-16, the assessee paid Rs.25,50,000/- to Matha Infratech on 05-09-2014 after deducting TDS of 1%. These payments were directly made to nominees of the subcontractor viz., Mr. Sharanappa Patil Anwari, Mr. Amaregowda and Mr.Mallikarjun G., TDS as applicable is deducted on these payments. The TDS is remitted to the department. The assessee had carried this work in the earlier years also with Matha Infratech, since the subcontract agreement was entered with them in 2010. The assessee was due to pay Matha Infratech for the work executed by them earlier and this amount they had shown in the books as liability. The liability as per books as on 31st March 2015 was Rs.9,36,597/-The AO has disallowed expenditure of Rs.25,50,000/- and added back Trade payables of Rs.9, 36, 597/-.

4.6 She submitted that as explained in the above paragraphs in case of S K Infrastructure, the AO on similar grounds has disallowed the payments made and added back the Trade payable in this case also. The prohibition of giving work on subcontract is an arrangement between Client and the assessee. If the assessee has given these works on subcontract, it is the violation of terms of Contract agreement with the client. Only the client can question the assessee for not obtaining any prior permission or for violation of the terms of the contract. The Learned Officer has no jurisdiction to question the assessee on the violation of this clause and give this as one of the reason to treat Matha Infratech as 'Shell Entity'. Non filing of Annual returns to the Registrar of Companies is given as another reason, which is also not justified as it is the responsibility of the subcontractor to comply with their legal requirements. In this case also the subcontractor has deregistered his VAT registration on 30-04-2014. The assessee entered into Sub Contract agreement with Matha Infratech in 2010 and they have also registered with VAT in the same year as 'Works Contractor". Being a Company incorporated

under the Companies Act 1956, all the legal compliances should have been complied by subcontractor and the assessee is not responsible for noncompliance. AO in his order has made a mention "The fact that the company was started in 2010 and till 2017 it did not file any returns, is another evidence that the company is not doing any work. Hence M/S Matha Infratech Pvt. Ltd was also seen to be a shell entity" is absolutely baseless and does not hold test of law. Hence, she submitted that disallowance of expenditure of Rs.25,50,000/- and add back of Trade Creditors of Rs.9,36,597/- with regard Matha Infratech Private Limited is unjustified and the same may be set aside.

4.7 The ld. A.R. for the Assessee pleaded that the disallowance of payments made to S K Infrastructure of Rs.71,40,000/- and Matha Infratech Private Limited Rs.25,50,000/- to be allowed as Expenditure and add backs of Trade Payables Rs.54,11,497/of S K Infrastructure and Rs.9,36,597/- of Matha Infratech may be deleted.

4.8. The ld. A.R. submitted that the total revenue from the operations was Rs.1,53,83,082/- in the assessment year under consideration and the assessee declared loss of (-Rs.51,96,168/-). However, the ld. AO made addition of Rs.96.90 lakhs by treating the sub-contract as a bogus and also treated Rs.63.48 lakhs payable to S.K. Infrastructures at Rs.54.11 lakhs and Matha Infratech Pvt. Ltd. at Rs.9.37 lakhs as cessation of liability. Thus, the computed income of Rs.1.08 Crores, which resulted in 71% net profit rate, which is impossible in this kind of business. Further, without prejudice to the above argument, ld. A.R. submitted that even if it is considered as sub-contract payments are not genuine, it is not possible to treat the entire sub-contract as bogus and she submitted that net profit on such contract may be estimated. With regard to cessation of liability of Rs.63.48 lakhs, she submitted that these are genuine trade debts emanated from the sub-contract once addition is made on account of sub-contract treating it as bogus. There cannot be any

further addition on this count, otherwise, it amounts to double addition. She relied on the judgement of Hon'ble Madras High Court in the case of CIT Vs. SPL Infrastructure Pvt. Ltd. in TCA No.766 of 2017 dated 7.8.2020.

5. On the other hand, ld. D.R. submitted that the sub-contract charges are bogus as such there cannot be allowance of any expenditure u/s 37 of the Act and consequently, the debts shown in their liability as current liability also considered as cessation of liability u/s 41(1) of the Act and same to be confirmed.

6. We have heard the rival submissions and perused the materials available on record. As rightly pointed out by the ld. A.R., similar issue came for consideration before Hon'ble Madras High Court in the case of M/s. SPL Infrastructure Pvt. Ltd. in TCA No.766/2017 dated 7.8.2020, wherein their Lordship held as under:

“5. We have heard both the parties and perused the material on record. In this case, it is admitted fact that 14 persons have furnished confirmation and some of the parties in response to summons issued to them have furnished the copies of income-tax return and also copies of bank account. Some of the parties also confirmed that they do not have invoice copies and maintain only Method book which was returned by the assessee. The copy of M.Book gave details of work done for a particular period, measurement up to the date of <http://www.judis.nic.in> Order dt. 7.8.2020 in TCA 766 of 2017 CIT v. SPL Infrastructure Pvt. Ltd. work with the signature of supervisor of the company. 11 parties have sent the details from far off places to the Assessing Officer through courier. However, there was no response from two parties. The assessee has taken the road laying work and also completed that work. Most of the payments are not supported by bills issued by the above parties. On the above reasons, the Assessing Officer disallowed Rs.4,41,08,210/-. However, the CIT(A) considering the nature of business of the assessee and also chances of inflated expenses, sustained the disallowance to 10% of above expenditure. As seen from the fact brought on record that the assessee's total turnover for the assessment year under consideration is at Rs.3334.16 lakhs against which the assessee declared gross profit of 14.21% and net profit at 3.83%. When we compare the turnover of gross profit and net profit of the present assessment year with other assessment years it is at higher side. This can be seen from the below mentioned <http://www.judis.nic.in> Order dt. 7.8.2020 in TCA 766 of 2017 CIT v. SPL Infrastructure Pvt. Ltd. table:

Rs. in Lakhs

Y.E.	31.3.05	31.3.06	31.3.07	31.3.08	31.3.09	31.3.10
Turnover	31.33.38	2760.71	3527.99	6680.59	11585.30	3334.16
G.P.	253.47	247.37	352.46	436.04	625.25	473.93
Depn.	52.96	57.65	87.09	104.58	96.44	159.49
Interest	68.94	80.95	166.81	197.47	190.04	186.91
N.P.	131.57	108.77	98.56	133.99	338.77	127.53
GP as % of TP	8.09	8.96	9.99	6.52	5.40	14.21
NP as % of TO	4.20	3.94	2.79	2.01	2.92	3.83

Further, it is also admitted fact that the payment to above parties was subject to TDS and paid by cheques and the assessee has maintained the M. book which is signed by the sub-contractors. The only discrepancy noticed by the Assessing Officer is that the payments are not supported by the bills raised by the parties and only self-made vouchers were maintained by the assessee. In our opinion, considering the nature of work carried on by the assessee, there is no question of not incurring of expenditure by the assessee to carry on the road work contracts and the work is mentioned in the M <http://www.judis.nic.in> Order dt. 7.8.2020 in TCA 766 of 2017 CIT v. SPL Infrastructure Pvt. Ltd. book maintained by the assessee and counter signed by the sub- contractors. However, there is chances of inflating the expenditure for which the CIT(A) has, already disallowed 10% of the expenditure claimed by the assessee to the extent of Rs.4,41,08,210/-. Hence, the contention of the ld. DR that the entire amount of Rs.4,41,08,210/- is to be disallowed cannot be appreciated as held by the Tribunal in the case of EDAC Engineering Ltd vs ACIT, 149 ITD 341, wherein held that if expenditure claimed was not supported by proper evidence and some deficiency persist in evidence, part expenditure is disallowed on estimated basis. Being so, by placing reliance on the above decision of the Tribunal, the CIT(A) is justified in disallowing only 10% of the sub-contract expenses not supported by proper bills. This ground of the Revenue is dismissed.

6.1 Further, Coordinate Bench of the Tribunal in the case of Total Environment Building Systems Pvt. Ltd. in ITA No.352/Bang/2023 for the assessment year 2012-13 vide order dated 18.12.2023 while discussing about the taxing of cession of liability observed as under:

“10. We have heard the rival submissions and perused the materials available on record. In the present case, it is an admitted fact that an amount of Rs.39,65,829/- has been shown as outstanding in the books of accounts of assessee and also in its financial statements. This amount has not been written off by the assessee in its books of accounts and there is also no confirmation that the other party to whom the assessee is owing has written off these debts in their books of accounts. As held by Hon’ble

Supreme Court in the case of CIT Vs. Sugauli Sugar Works Pvt. Ltd. that unless the debt has been written off in the books of accounts of both the assessee, it cannot be said that "that cease to exist". The cessation of liability may occur either by reason of the operation of law i.e. on the liability of becoming unenforceable law by the creditor and the debtor declaring unequivocally his intention not to honour his liability when payment is demanded by the creditor or contact between the parties or by the discharge of the debt, the debtor making payment there of to his creditor. As discussed in earlier para, in the present case, the assessee has not written off the same in its books of accounts and it cannot be said that the debt ceased to exist. Being so, we are of the opinion that in the assessment year under consideration, this amount cannot be considered as cessation of liability u/s 41(1) of the Act. This ground of appeal of the assessee is allowed."

6.2 In the present case, the assessee has declared loss of Rs.51.96 lakhs out of total turnover of Rs.1,53,83,082/-. The ld. AO made addition of Rs.1,40,94,505/- towards bogus sub-contract receipts and by invoking the provisions of section 41(1) of the Act. In our opinion, addition of Rs.1,40,94,505/- out of sales receipt of Rs.1,53,83,082/- is highly impossible and we cannot agree with that income determined by the ld. AO and confirmed by the NFAC. On other hand, the assessee also not maintained proper books of accounts and also not produced any of its past history with regard to net profit declared by the assessee. In our opinion, the books of accounts of the assessee are not reliable. It has not deduced the true profit of assessee's business. In view of this, after considering the judgement of Hon'ble Madras High Court in the case of M/s. SPL Infrastructure Pvt. Ltd., we reject the books of accounts of assessee and accordingly, we estimate the net profit of the assessee at 8% on revenue declared by the assessee at Rs.1,53,83,082/- which worked out at Rs.12,30,646/- as net income from business as against the loss declared by the assessee at Rs.51,96,168/- in the assessment year under consideration. Thus, the assessee is not entitled for any further deduction towards any expenditure including depreciation, if any claimed by the assessee and the ld. AO is directed to determine the income of the assessee from business (i.e. other than income from

other sources) for the assessment year under consideration at Rs.12,30,646/-. Further, interest u/s 234A, B, C & D are consequential and mandatory in nature to be computed accordingly. Ordered accordingly.

7. In the result, appeal of the assessee is partly allowed.

Order pronounced in the open court on 8th July, 2024

Sd/-
(Beena Pillai)
Judicial Member

Sd/-
(Chandra Poojari)
Accountant Member

Bangalore,
Dated 8th July, 2024.
VG/SPS

Copy to:

1. The Applicant
2. The Respondent
3. The CIT
4. The DR, ITAT, Bangalore.
5. Guard file

By order

Asst. Registrar,
ITAT, Bangalore.