

आयकर अपीलीय अधिकरण, इंदौर न्यायपीठ, इंदौर
IN THE INCOME TAX APPELLATE TRIBUNAL
INDORE BENCH, INDORE
BEFORE SHRI VIJAY PAL RAO, VICE PRESIDENT
AND
SHRI B.M. BIYANI, ACCOUNTANT MEMBER

ITA No.73/Ind/2024
Assessment Year: 2017-18

CMM Keti JV, 108, Shalimar Corporate Center, 8-B, South Tukoganj, Indore. (Assessee/Appellant)	<u>बनाम/</u> <u>Vs.</u>	Income-tax Officer, 1(3), Indore. (Revenue/Respondent)
PAN: AAKFC7524K		
Assessee by	Shri Shashank Sharma, CA and Shri Prakash Gupta, CA	
Revenue by	Shri Sanjeev H. Bhagat, Sr. DR	
Date of Hearing	11.12.2024	
Date of Pronouncement	20.01.2025	

आदेश / O R D E R

Per B.M. Biyani, A.M.:

Feeling aggrieved by appeal-order dated 22.11.2023 passed by learned Commissioner of Income-Tax (Appeals)-NFAC, Delhi ["CIT(A)"] which in turn arises out of assessment-order dated 31.12.2019 passed by learned ITO-1(3), Indore ["AO"] u/s 143(3) of Income-tax Act, 1961 ["the Act"] for Assessment-Year ["AY"] 2017-18, the assessee has filed this appeal.

2. The background facts leading to present appeal are such that the assessee is a partnership firm engaged in the business of civil construction/ infrastructure projects including work-contracts service. For AY 2017-18, the assessee filed return

declaring a total income of Rs. 310/-. The case of assessee was selected for scrutiny for the reason of "High Ratio of Refund to TDS". The AO issued notices u/s 143(2) followed by questionnaires/show-cause notices u/s 142(1) which remained uncompiled or partly compiled by assessee. Ultimately, the AO passed assessment-order after making an addition of Rs. 1,03,58,079/- as under:

"7. Addition on account of Business Income:

Thus, the assessee was requested vide this office notice u/s 142(1) dated 10-12-2019, dated 21-12-2019 & 26-12-2019 to produce books of account for F.Y. 2016-17. But the assessee failed to produce books of account before the undersigned so as to establish genuineness of Income & Expenditure.

The assessee did not furnish information/details as requested u/s 142(1) dated 21-12-2019 & 26-12-2019.

It is also show-cause, vide above said notice u/s 142(1) dated 26-12-2019 that in absence of books of account, bills, vouchers, why the net profit @ 2% of total turnover (i.e. Rs. 51,79,03,950/-) which comes to Rs. 1,03,58,079/- shall not be ascertained and treated as your business income. In absence of compliances of the assessee, I have no option but to ascertain business income @ 2% of total turnover (i.e. Rs. 51,79,03,950/-) which comes to Rs. 1,03,58,079/-. Hence business income of the assessee has been determined at Rs. 1,03,58,079/-. I am satisfied that the assessee has mis-reporting of its income to the tune of Rs. 1,03,58,079/-. Hence penalty proceedings u/s 270A(9) is initiated separately."

3. The AO initiated penalty proceeding u/s 270A(9) as noted in preceding para. Further, the AO also observed that the assessee has made most of the payments to CMM Infraprojects Ltd. ["CMM"], a partner of assessee-firm and the payments so made were covered by section 40A(2)(b) but no reporting qua such transactions was made in Point No. 23 of Tax Audit Report, therefore the AO initiated penalty proceeding u/s 271B. Further, the AO also initiated penalty proceedings u/s 272(1)(d) for non-compliances of notices u/s 142(1). This way, the AO initiated various penalty proceedings u/s 270A(9), 271B and 272(1)(d).

4. During first-appeal, the CIT(A) passed following order upholding the addition made by AO:

“8. Ground no.1 is relating to addition of Rs. 1,03,58,390/- being 2% of the turnover as the income of the appellant. During the appellate proceedings also the appellant has not made any submissions with reference to the applicability of the provisions of section 40A(2)(b) of the Act nor any justification was given as to why 99.95% of the contract receipts were given to the sub-contractor and claimed expenditure in its P&L A/c. No agreement was filed relating to the sub-contractor as to what compelled the appellant to make such huge payments to the sub-contractor without ensuring adequate profitability for the appellant.

8.1 During the appellate proceedings, only the claim of the appellant was that the AO has taxed the income of the appellant 2% of the turnover merely on the basis of the guess work. The other plea taken was the books of the appellant are audited and the payments have been made to the sub-contractor after deducting tax u/s. 194C of the Act. The appellant did not produce the books before the AO nor did the appellant furnish any details relating to the payments made to the sub-contractor whether attracted the provisions of Section 40A(2)(b) of the Act. In fact the AO has given a finding that the audit report is totally silent in respect of payments u/s. 40A(2)(b) of the Act in spite of the fact that the appellant has actually made the payments to the persons specified in Section 40A(2)(b) of the Act.

8.2 For the sake of clarity, the material part of section 40A(2)(a) is reproduced as under:

(2)(a) Where the assessee incurs any expenditure in respect of which payment has been or is to be made to any person referred to in clause (b) of this sub-section, and the Assessing Officer is of opinion that such expenditure is excessive or unreasonable having regard to the fair market value of the goods, services or facilities for which the payment is made or the legitimate needs of the business or profession of the assessee or the benefit derived by or accruing to him there from, so much of the expenditure as is so considered by him to be excessive or unreasonable shall not be allowed as a deduction.”

8.3 Admittedly, in absence of any details produced by the appellant, the expenditure is deemed to have been incurred by making payment to the person specified in Section 40A(2)(b) of the Act. The only question, therefore, is whether the expenditure to the extent it has been disallowed is excessive or unreasonable having regard to the services or facilities for which the payment is alleged to have been made or the legitimate needs of the business of the appellant or the benefit derived or accruing to it therefrom. It is obvious that if the same be excessive or unreasonable having regard to these specified circumstances, then to the extent it is excessive or unreasonable, it shall not be allowed as a deduction. By making an addition of 2% of the turnover, the AO has effectively restricted the payments made to the sub-contractors to 97.95% of the receipts. The appellant is a partnership firm and is engaged in doing business, which is obviously for earning profits. It is a separate entity for taxation purposes and the payments even though made to the sister concerns have to be made at arm's length as if the payments are made to third/unrelated parties. In the instant case, the appellant by making payment at 99.95% of the contract receipts to the sub-contractor has indulged in making excessive or unreasonable expenditure and hence the same cannot be allowed.

8.4 The appellant in its submissions has referred to certain cases wherein it has been held that lumpsum/adhoc disallowance cannot be made. However, in my opinion the disallowance made by the AO by estimating the income @ 2% of the turnover was justified

in the facts and circumstances of the appellant's case. It is not a lumpsum or adhoc disallowance. As the appellant has not produced the relevant details sought by the AO in spite of the fact that sufficient time and opportunity was given, the AO was constrained to make the said disallowance. Reliance is placed on the decision of Hon'ble MP High Court in the case of Ganesh Soap Works vs. CIT 161 ITR 876 (MP). In the said case, the Hon'ble High Court held that the payments made for the considerations other than business and in excess of fair market value of services rendered was a question of fact and disallowance made by the lower authorities of such excess amount was upheld. If the AO has accepted the appellant's return in the subsequent assessment year cannot be the reason that it should be accepted in the impugned assessment year as well as principle of Res Judicata is not applicable to the income tax assessments. Perhaps the AO in the subsequent year has not examined the case of the appellant in proper perspective including the applicability of the provisions of section 40A(2)(b) of the Act.

8.5 In view of the above facts of the appellant's case and the judicial pronouncement of the Jurisdictional High Court I come to a conclusion that the amount paid by the appellant to M/s. CRM Infra Projects Ltd, was definitely higher than the actual market value. The said payment was not certainly at arm's length. Therefore, I hold that the arm's length payment could reasonably be estimated at 97.95% of the contract receipts and hence warranting disallowance of 2% (as the appellant has already offered 0.05% in the return). Arithmetically, the disallowance made by the AO of Rs. 1,03,58,390/- is sustained. Ground no. 1 is dismissed."

5. Aggrieved by orders of lower-authorities, the assessee has come in appeal before us.

6. The grounds raised by assessee are as under:

- "1. The Hon'ble Commissioner of Income-tax (Appeals) has erred in law by not allowing the appellant a reasonable opportunity of being heard by not allowing physical hearing/vitual hearing which is against the Principle of Natural Justice.*
- 2. The Hon'ble Commissioner of Income-tax (Appeals) has erred in invoking the provisions of section 40A(2)(b).*
- 3. The Hon'ble Commissioner of Income-tax (Appeals) has erred in adding flat rate of 2% of turnover on ad-hoc basis solely on assumption and presumption which is baseless and not justifiable."*

7. In Ground No. 2 & 3, the assessee has precisely challenged the addition of Rs. 1,03,58,079/- made by AO by estimating 2% profit on turnover and upheld by CIT(A).

8. Apropos to these grounds, Ld. AR for assessee firstly made a brief submission of assessee's business model. He submitted that the assessee, a partnership firm, is a joint venture/special purpose vehicle established by two companies as partners, the main partner being CMM holding 60% share. The assessee was created only to satisfy bidding requirement of infraprojects to be taken from Govt. Therefore, the business model of assessee is such that it got contracts/contract revenues from Govt. and in turn it made back-to-back sub-contracts/sub-contract payments to CMM.

9. Then, Ld. AR drew us to various pages of Paper-Book to show following facts:

- (i) That the assessee filed audited accounts to AO (Page 126-128 of Paper-Book). The audited P&L A/c clearly shows contact receipts of Rs. 51,79,03,950/- on credit side. On debit sides, there are items of opening stock of Rs. 1,93,225/-, sub-contracts payments of Rs. 51,76,43,015/- made to CMM, audit fee of Rs. 7,500/-, Bank charges of Rs. 439/- and Interest payment of Rs. 59,460/-; leaving a net profit of Rs. 311/-.
- (ii) That the assessee filed reply dated 18.12.2019 to AO (Page 105-134 of Paper-Book) explaining various queries raised in notice dated 10.12.2019 u/s 142(1). Vide Para 9 of same, the assessee filed details of Contract Payments of Rs. 51,76,43,015/- made to CMM and Interest expenditure of Rs. 59,460/-. The Ledger A/cs of these expenses were also submitted to AO (Page 112-115 of Paper-Book). The payments of Rs. 51,76,43,015/- made to CMM is breaked-up for three projects consisting of Jawasa Project - Rs.

12,82,73,199/- (+) Nadiagaon Project – Rs. 17,94,46,572/- (+) Ambah Pinaht Project – Rs. 20,99,23,244/-.

(iii) That the assessee deducted TDS out of all payments of Rs. 51,76,43,015/- made to CMM which are evident from Page 2 of Form No. 26AS of CMM filed at Page 231 of Paper-Book and the details of TDS filed to CIT(A) at Page 99 of Paper-Book.

10. Therefore, Ld. AR contended, the AO ought to have considered assessee's facts and refrained from making any intervention with the income declared in return. Ld. AR submitted that the AO is wrong in assessing business income of assessee on adhoc basis @ 2% of turnover and thereby making a hefty addition of Rs. 1,03,58,079/-; the addition made by AO must be deleted.

11. Then, Ld. AR assailed the order of CIT(A). He submitted that the CIT(A) has precisely observed that the payments made to CMM attracted section 40A(2) and thereby upheld AO's addition on the strength of section 40A(2) but the AO has made adhoc addition @ 2% of turnover. He submitted that the AO has nowhere raised any question qua section 40A(2). Therefore, the CIT(A)'s approach is patently and clearly wrong.

12. Ld. AR also drew us to the financial/income-tax data of CMM. He submitted that for AY 2017-18 under consideration, CMM declared turnover as high as Rs. 144.32 crores (inclusive of receipts of Rs. 51,79,03,950/- from assessee), net profit of Rs. 5.05 crores from operational activity and paid income tax of Rs. 1.62 crores which approximately comes to 32%. Therefore, the tax paid by CMM is in line with

the tax rate applicable to assessee which shows that there is no tax evasion because of sub-contracting of work by assessee to CMM.

13. Per contra, Ld. DR for revenue made following submissions:

- (i) The assessee has made non-compliances of notices dated 21.12.2019 & 26.12.2019 issued by AO and failed to file the details required by AO. The AO has also noted that the assessee has failed to file complete books of account. Therefore, the AO had no option except to assess business income at 2% of turnover.
- (ii) That the CIT(A) has passed a vehement order giving detailed reasoning for application of section 40A(2) to assessee's case and upheld AO's order.
- (iii) That the orders passed by lower-authorities are proper in the facts of assessee, hence the same must be upheld. Alternatively, the case should be remanded back to AO with a direction to assessee to submit clarifications sought by AO.

14. We have considered rival submissions of both sides and perused the case record including orders of lower authorities. The grievance of assessee is the addition of Rs. 1,03,58,079/- made by AO. The AO has made this addition by estimating net profit of assessee @ 2% on turnover of Rs. 51,79,03,950/-. The reason of making such addition, as narrated by AO, in assessment-order is non-furnishing of information required by him through notices dated 21.12.2019 & 26.12.2019. It is noteworthy that the assessee is a partnership firm and has made a total payment of Rs. 51,76,43,015/- to one of its partners "CMM" against turnover of

Rs. 51,79,03,950/-. The other expenses are very less and aggregate to just Rs. 2,60,624/-. Accordingly, the assessee has declared a negligible net profit of Rs. 311/-. Although the assessee has filed letter dated 18.12.2019 in response to notice dated 10.12.2019 issued by AO but the AO, after consideration of assessee's letter, still required more clarifications from assessee and therefore issued notices dated 21.12.2019 & 26.12.2019 but the assessee did not file the clarifications sought by AO. That apart, the AO has also noted in Para 4 of assessment-order that in reply dated 18.12.2019, the assessee stated that books of account are being produced but in fact the assessee never produced books of account during entire assessment proceedings. In Para 4 of notice dated 26.12.2019, the AO specifically show-caused assessee about non-reporting of payments made to CMM in Tax Audit Report, although mentioning for initiation of penalty u/s 271B, but the fact remains that the assessee made non-compliance of notice issued by AO and did not file any reply. Had the assessee filed reply to AO's query, the AO would have been in a position to take appropriate call for payments made to CMM from the angle of section 40A(2). Therefore, due to non-compliant attitude of assessee, the AO as a last measure adopted 2% net profit on turnover and made impugned addition. Faced with this situation, we agree with Ld. DR's prayer that the present case must be remanded to AO for adjudication afresh after hearing assessee. We may also add here that in *Ground No. 1*, the assessee has raised a grievance that the CIT(A) has erred by not giving the assessee a reasonable opportunity of physical/virtual hearing which is against the principle of natural justice. Although Ld. AR for assessee has not made any oral submission qua this ground during hearing, in the Written-Submission dated 08.07.2024, a detailed submission has been made on Page 4 to 7 with regard to

Faceless Appeal Scheme, 2021 and certain judicial rulings and thereafter the assessee has requested to set aside the order passed by CIT(A). If the request of assessee is taken into account, it would require us to remand this matter to CIT(A). However, in the facts of case, we are remanding this matter down-the-line to AO which would be a better solution to assessee and also meet the request of Ld. DR for revenue. For these reasons, this matter is remanded to AO with a direction that the AO shall give adequate opportunities to assessee and pass order afresh after considering submissions of assessee. Needless to mention that the AO shall not be influenced by his previous order in any manner. The assessee is also directed to make compliances of the hearings to be fixed by AO and do not seek unnecessary adjournments.

15. Resultantly, this appeal is allowed for statistical purposes.

Order pronounced by putting up on notice board in terms of Rule 34 of ITAT Rules, 1963 on 20/01/2025
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Sd/-

(VIJAY PAL RAO)
VICE PRESIDENT

Sd/-

(B.M. BIYANI)
ACCOUNTANT MEMBER

Indore

दिनांक /Dated : 20/01/2025

Patel/Sr. PS

Copies to: (1) The appellant
(2) The respondent
(3) CIT

- (4) CIT(A)
- (5) Departmental Representative
- (6) Guard File

By order

Sr. Private Secretary
Income Tax Appellate Tribunal
Indore Bench, Indore