

**IN THE INCOME TAX APPELLATE TRIBUNAL,
DELHI BENCH 'B' NEW DELHI**

**BEFORE : SHRI H.S. SIDHU, JUDICIAL MEMBER &
SHRI L.P. SAHU, ACCOUNTANT MEMBER**

**ITA No. 3710/Del./2013
Asstt. Year : 2009-10**

D.C.I.T., Circle 32(1),
New Delhi.

vs.

Deepsons Southend,
M-10, South Extension-II,
New Delhi.
[PAN:AACFD1758J]
(Respondent)

(Appellant)

Appellant by : Smt. Parwinder Kaur, Sr. DR
Respondent by : Sh. Prakash Yadav, Adv. &
Sh. S.C. Malhotra, C.A.

Date of hearing : 11.09.2015
Date of pronouncement : 30.10.2015

ORDER

Per L.P. Sahu, Accountant Member:

This is an appeal filed by the Revenue against the order dated 06.03.2013 of Id. CIT(A)-XXVI, New Delhi for the assessment year 2009-10.

2. The brief facts of the case are that the assessee is a partnership firm and carrying on the business of trading in readymade garments and accessories. The assessee filed return of income on 20.09.2009 declaring nil income which was processed u/s. 143(1) of the IT Act on same income. The case was

selected for scrutiny u/s. 143(2) and notice was issued on 20.08.2010. Subsequently, notice u/s. 142(1) was also issued time to time. The Assessing Officer made various additions and completed the assessment order. The assessee challenged the assessment order before the Id. CIT(A) who allowed the appeal of the assessee vide the impugned order. It is this order which has been challenged by the Revenue in this appeal on the following grounds :

“1. Whether the CIT(A) is justified in admitting the additional evidences filed by the assessee at appellate stage in spite of the fact that assessee does not fulfill the mandatory conditions of rule 46A.

2. Whether the CIT(A) has erred in the facts and circumstances of the case in holding that the case of assessee is not a case where new firm had been constituted or had taken over any old firm and carry forward and set off brought forward losses/unabsorbed depreciation.

3. Whether in the facts and circumstances of case the CIT(A) is justified in deleting the addition of Rs.3,00,000/- made on account of disallowance of expenses claimed for representing the case of assessee in block assessment proceedings.

4. Whether the CIT(A) is justified in the facts and circumstances of the case in allowing relief of Rs.24,379/- out of the addition of Rs.57,212/-.

5. Whether in the facts and circumstances of case the CIT(A) is justified in deleting the addition of Rs.16,04,832/- holding that the expense claimed was not towards penalty.

6. Whether in the facts and circumstances of case the CIT(A) is justified in deleting the addition of Rs.60,79,928/- made u/s. 36(1)(iii).

7. Whether in the facts and circumstances of case the CIT(A) is justified in deleting the addition of Rs.53,374/- and in holding that the said expense was for business purpose.

8. Whether in the facts and circumstances of case the CIT(A) is justified in deleting the addition of Rs.26,00,000/- made u/s. 68 of the I T Act, 1961."

3. The ld. DR relying upon the order of the Assessing Officer, submitted that the ld. CIT(A) was not justified in admitting the additional evidences ignoring the fact that the assessee did not fulfill all the conditions of Rule 46A. He also submitted that the ld. CIT(A) has wrongly deleted various additions made by the AO ignoring the facts that the additions were made by the AO on cogent reasons based on the record. On the other hand, the ld. AR of the assessee relied upon the order of the ld. CIT(A) on various grounds.

4. We have heard the rival submissions, perused the material available on record and the orders of the authorities below.

5. As far as ground No. 1 raised by the Revenue is concerned, the record reveals that the assessee moved an application dated 18.05.2012 u/r 46A before the ld. CIT(A) with the request to admit the additional evidences annexed with the written reply of the assessee in the form of copy of block assessment order, extracts for Master Plan for 2021, copies of balance sheets,

letter dated 13.12.2011 and confirmation, IT return, PAN of the creditor etc. The written submission supported by documentary evidence was forwarded to the AO for his examination and comments and the AO furnished remand report dated 26.06.2012 on the same. The copy of the remand report of the AO was also provided to the Assessee who also filed rejoinder before the Id.CIT(A). After considering the contentions of both the parties, the Id. CIT(A) observed that the additional evidences filed are relevant and vital that would go to root of the matter while deciding the issues to which they relate. He, therefore, admitted the same on record. We do not find any incongruity in this conclusion of the Id. CIT(A). The Id. DR failed to point out as to which of the conditions of Rule 46A was not fulfilled by the assessee. Therefore, ground No. 1 of the Revenue being devoid of merits, is liable to be dismissed.

6. Coming to ground No.2, it is borne out on record that the assessee is a partnership firm and deed of partnership was executed on 02.07.1999 which was reconstituted on 22.11.1999 and again on 02.04.2007 and the changes were made only in the profit sharing ratio. The firm was running in losses which were being carry forwarded year to year. As per computation of income, the assessee had shown business loss of Rs.80,54,133/- and has claimed set off of this loss against income of Rs.1,48,80,947/- shown from house property.

The remaining house property income of Rs.68,26,815/- was also set off by adjusting the brought forward unabsorbed depreciation of the same amount and thus has shown nil income in the return. On 02.04.2007, the firm was reconstituted as a going concern concept, which has taken over the business of old firm also named as M/s. Deepsons Southend constituted under the deed of partnership dated 22.11.1999. The Assessing Officer observed that the profit sharing ratio in the new partnership deed executed on 02.04.2007 is different from the profit sharing ratio of the earlier firm having the same name and there is a new source of income in the hands of the new firm which shows existence of a new firm on 02.04.2007, irrespective of the fact that the name and partners of both the firms are same. He, therefore, observed that the case of the assessee is not covered by the provisions of section 187 and the brought forward losses of another firm is not allowed to be set off in terms of section 78 of the Income Tax Act. The Id. CIT(A) accepted the contention of the assessee and brought forward loss was allowed to be set off, holding that in the instant case, there was only change in the profit sharing ratio of the partners, which was merely a change in the terms and conditions of the partnership as the same partners continued to carry on the business. He also observed that this was not a case where new firm has been constituted or had

taken over any old firm. Therefore, the case of the assessee clearly is covered under section 187 of the Act and not u/s. 78 of the Act as held by the AO.

7. Having considered the rival submissions on this issue, we find that the Id. CIT(A) has rightly allowed the appeal of the assessee on this issue because mere change in the profit sharing ratio would not amount to reconstitution of the partnership for the purpose of section 78 of the Act. It is not in dispute that all the partners after reconstitution of firm remained same and there is no instance of any incoming or outgoing partner. It is also borne out on record that the firm was incurring continuous losses and filing returns of income as such. The Id. Assessing Officer has invoked the provisions of section 78 of the Act, which reads as under :

“78. (1) Where a change has occurred in the constitution of a firm, nothing in this Chapter shall entitle the firm to have carried forward and set off so much of the loss proportionate to the share of a retired or deceased partner as exceeds his share of profits, if any, in the firm in respect of the previous year.

(2) Where any person carrying on any business or profession has been succeeded in such capacity by another person otherwise than by inheritance, nothing in this Chapter shall entitle any person other than the person incurring the loss to have it carried forward and set off against his income.”

A perusal of above provisions shows that if there is change in the constitution of a firm by way of a retirement or death of any partner, then the firm is not entitled to have carried forward and set off so much of the loss proportionate to the share of a retired or deceased partner which exceeds his share of profits. In the instant case, the reconstitution of the firm is not made as a result of retirement of any partner or death of any partner. As a matter of fact, the reconstitution of the partnership was made only as a result of changes in the profit sharing ratio amongst the partners. Therefore, in our considered opinion, the Id. CIT(A) has rightly allowed carry forward losses to be set off, as claimed by the assessee. Accordingly, this ground of appeal of the Revenue also deserves to be dismissed.

8. In ground No. 3, the Revenue has challenged the deletion of disallowance of Rs.3,00,000/- made by the AO u/s. 37(1) of the Act. In the assessment proceedings, the AO noticed that the assessee had paid a sum of Rs.3,00,000/- to M/s. S.R. Kapoor & Company for appearing in block assessment proceedings. The AO observed that since no block assessment order was passed in the case of assessee firm, the expenses booked by the assessee might have related to the block assessment completed in the case of the partner or in the case of other concern of the group. He, therefore,

disallowed the expenses u/s. 37(1) of the Act. The Id.CIT(A) allowed the claim of assessee stating that the appeals against the block assessment proceedings are pending at the stage of Tribunal and the bill of the consulting firm narrating the legal fee for representation in block assessment proceedings, is addressed to the assessee firm.

9. The Id. DR contended that the block assessment proceedings, initiated as a result of search dated 26.02.02, stood completed on 27.02.2004 and even the appeal before the CIT(A) stood disposed of on 20.12.2004. Therefore, there is no reason to make payment in the A.Y. 2009-10 with respect to such proceedings which stood completed 3-4 years back. On the other hand, the Id. Counsel for the assessee contended that the appeals against block assessment proceedings are still pending with ITAT and therefore, it cannot be said that the impugned amount paid to the consulting firm during the year was not for the purpose of business of the firm. The block assessment was completed and quantum of liability was not fixed by the consulting firm therefore provision could not be made, whenever he issued bill we paid it on 11/02/2009 by issuing cheque.

10. Having considered the rival submission, we find that the narration made on bill No. SRK/4/(08-09)/154 dated 30.07.2008 is *“To fee for representation in Block assessment proceedings before various Income-tax authorities (In response to notices)”*. We have perused the block assessment order, which stood completed on 27.02.2004. Even the appeals against the block assessment proceedings stood disposed of on 20.12.2004. This shows that the work assigned to the consulting firm was completed in F.Y. 2004-05. But the liability was not created due to non issuing of bill by the Consulting Firm . We are agree with the arguments made done by Ld. AR. . The assessee has maintained the books of account in mercantile system and he did not make any provision in this regard in his books of account in earlier years. There is no agreement on record to indicate that the assessee may make such payments whenever he thinks fit. We, therefore, find that the ld. CIT(A) has rightly deleting the disallowance made by the AO. Accordingly, ground No. 3 of appeal of Revenue is dismissed.

11. Ground No. 4 challenges the relief of Rs.24,379/- given by the CIT(A) out of the addition of Rs.57,212/- made by the AO. The facts relating to this ground of appeal are that during the assessment proceedings, the AO noticed that the assessee had debited expenses of Rs.3,95,353/- towards repair of the building,

out of which the expenses attributable to property income were shown at Rs.1,80,000/- and remaining expenses of Rs.2,15,353/- were claimed against business income. The AO, however, considering the fact that out of the total five floors of the building, three floors have been let out during the year and remaining two were used by assessee firm, apportioned these expenses in the ratio of 60:40 and allowed Rs.1,58,141/- against business income as against Rs.2,15,353/- shown by the assessee. Accordingly, the AO added the difference of Rs.57,212/- to the total income of the assessee, inasmuch as he disallowed expenses of Rs.2,37,212/- as attributable towards property income as against Rs.1,80,000/- shown by the assessee under this head. The Id. CIT(A) after considering the explanation of the assessee and the statement of repairs and maintenance furnished by assessee, observed that the actual expenses in respect of the repair and maintenance of building were Rs. 3,54,271/- and remaining expenses of less than Rs.5000/- amounting to Rs.40,633/- were for other repairs and maintenance. He, therefore, apportioned the expenses of Rs.3,54,721/- in the ratio of 60:40 and held the sum of Rs.2,12,833/- attributable towards property income and remaining expenses of Rs.1,82,521/- were allowed against business income, thereby giving relief of Rs.24,379/- to the assessee.

12. We have considered the rival submissions on the issue and we find that there is no good reason to interfere with the conclusion reached by the Id. CIT(A). The Id. CIT(A) while deciding this issue has taken into consideration the statement of repairs and maintenance as also the bills of repairs & maintenance submitted by the assessee, which could not be rebutted by the Id. DR before us. We therefore, find no error in the conclusion reached by the Id. CIT(A) on this count. Accordingly, ground No. 4 of Revenue's appeal is dismissed.

13. Ground No. 5 challenges the deletion of addition of Rs.16,04,832/- made by the AO on account of expenses pertaining to rates and taxes u/s. 37(1) of the Act. The assessee debited Rs.16,04,832/- on account of expenses incurred towards rates & taxes, out of which a sum of Rs.10,12,355/- were attributed towards property income and remaining amount of Rs.5,92,477/- was claimed against business income. The Assessing Officer disallowed all these expenses stating that the payments of Rs.16,04,832/- were made to MCD not by the assessee but by sister concern M/s. Deepsons Departmental Stores. It was also observed that these payments were not in the nature of house tax but were charges levied by MCD in respect of compounding and registration fee for commercial activities. The AO therefore, held that since these expenses were

in the nature of penalty imposed by MCD for illegal and unauthorized construction, these expenses were covered under the explanation to section 37(1) and were not allowable expenditure. The Id. CIT(A) deleted this disallowance observing that it is immaterial who makes the payment on behalf of the assessee. What is to be seen is that whether the payment relates to assessee or not and has been duly accounted for in the books of account. The Id.CIT(A) has also gone through the ledger account of rates and taxes in the assessee's books wherein Deepsons Departmental Stores was shown as creditor. The bills issued by MCD were also found in respect to the assessee's business premises. He further observed that the payments were made based on laws of the Government and in connection with the business. The bills or receipts of the payments nowhere show that the alleged payments were in the nature of penalty. He, therefore, deleted the disallowance.

14. Having considered the rival submissions on the issue, we find that the Id. CIT(A) has rightly allowed these expenditure. We do not find any error in the finding of CIT(A) that the impugned expenditure were incurred by the assessee irrespective of the fact the same were paid by his sister concern. The bills raised were in the name of assessee and in the ledger account of assessee, the sister concern is shown as creditor. The expenditures were in the nature of

annual commercial use charges, registration charges and regularization charges etc. The documentary evidences furnished by the assessee nowhere depict the nature of payment to be that of penalty in contravention of any law. In fact these payments were made in compensation to protect the asset which was being used for assessee's business for so many years. No good ground is made out on behalf of the Revenue to hold that the impugned payments were in the nature of penalty. Therefore, in our considered opinion the Id. CIT(A) has rightly reversed the conclusion of the AO. We find support from the decision of Hon'ble Delhi High Court in the case of CIT vs. Loke Nath & Co. (1984) 17 Taxmann 209 (Del) wherein it has been held that "*the expenditure of payment of compensation incurred by the assessee has to be regarded as an integral part of the profit earning process of the assessee.*" In view of this discussion, we dismiss ground No. 5 of the Revenue's appeal.

15. Grounds Nos. 6 & 7 challenge the deletion of addition of Rs.60,79,928/- on account of disallowance of interest and Rs.65,374/- as bank charges (mentioned in ground No. 7 as Rs.53,374/-). The AO after considering balance sheet, trading, profit & loss account of the assessee, disallowed these expenses observing that if the capital borrowed is not utilized for the purposes of the

business, the assessee will not be entitled to deduction under section 36(1)(iii) of the Act. He further held as follows :

“14(a). In the instant case also, perusal of the balance sheet reveal that the interest bearing fund borrowed from PNB have been given to partners from year to year without charging any interest from them. The partner’s capital account for all the three years are showing debit balance. The debit balance in partner’s capital account can be seen earlier year also. In the financial year ended 31.03.2007, the partner’s debit balance were Rs.3,79,25,886/- which is increased to Rs.4,70,72,619/- as on 31.03.2008. The balance is reduced to Rs.3,87,66,293/- as on 31.03.2009 because of crediting partner’s capital on account of the extra income the firm has generated from letting out three floors. Thus, in this case, the interest paid on borrowed fund is not on allowable expenses u/s. 36(1)(iii) since the borrowed fund is not used for the purpose of business.”

16. The Id. CIT(A) allowed the claim of the assessee on the ground that in preceding assessment years 2002-03 to 2006-07, on the identical facts, interest paid to the bank on the same loan and claimed as an expense was allowed. Therefore, considering the rule of consistency, the Id. CIT(A) deleted the addition made by AO on account of disallowance of interest and bank charges paid to the bank.

17. We have heard the rival submissions on the issue and have gone through the entire record available before us. In the assessment order, the AO has disallowed the interest expenditure of Rs.60,79,928/- paid to the bank and

expenditure incurred on bank charges of Rs.53,374/- on the ground that these expenditure were not made for the purpose of business. In this context, we think it appropriate to reproduce the balance sheet and trading, Profit & Loss account of three financial years, i.e., 2006-07, 2007-08 and 2008-09 as under :

Liabilities	As on 31.03.2007		As on 31.03.2008		As on 31.03.2009	
Loans						
Bank						
i) Punjab National Bank	5,16,43,177.57		4,74,95,887.49		2,89,73,467.80	
ii) Others	2,26,05,000.00	7,42,48,177.57	2,26,05,000.00	7,01,00,887.49	2,32,05,000.00	5,21,78,467.80
CURRENT LIABILITIES						
i). Sundry Creditors		2,02,98,806.83		3,62,53,520.91	2,97,68,976.95	
ii) Security deposit-Rent					2,03,49,000.00	5,01,17,976.95
		9,45,46,984.00		10,63,54,408.40		10,22,96,444.75
Asset						
Fixed assets						
As per schedule attached		5,21,88,134.42		5,38,67,280.42		5,31,63,781.40
Stock in hand						
At cost of market value whichever is less		21,80,601.00		36,20,382.00		36,47,295.00
Cash & Bank balances		1,79,676.65		3,14,970.65		
Cash in hand						1,98,192.90
Sundry debtors, loans & advances						
i) sundry debtors & advances	6,39,50800					
ii) Advances			45,977.81		3,56,544.00	
iii) Advance Income-tax					47,31,160.00	
iv) Security deposits-DVB	14,33,178.25	20,72,686.25	14,33,178.25	14,79,156.06	14,33,178.25	65,20,882.20
Partner's capital accounts						
As per schedule attached		3,79,25,806.08		4,70,72,619.27		3,87,66,293.10
		9,45,46,984.00		10,63,54,408.4		10,22,96,444.75

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The trading, profit and loss account of the assessee is as under :

	2009	2008	2007		2009	2008	2007
Opening stocks	36,20,382/-	21,80,601/-	36,23,918/-	Sales	43,60,738/-	57,14,034/-	78,35,579/-
Purchases	31,82,014/-	56,25,311/-	43,39,855/-	Closing stocks	36,47,295/-	36,20,382/-	21,80,601/-
Gross profit carried down	12,05,637/-	15,28,504/-	20,52,407/-				
	80,08,033/-	93,34,416/-	1,00,16,180/-		80,08,033/-	93,34,416/-	1,00,16,180/-
Establishment	1,86,717/-	2,12,783/-	1,70,333/-	Gross profit brought down	12,05,637/-	15,28,504/-	220,52,407/-
Electricity & water charges	5,71,269/-	9,50,507/-	6,01,918/-	Misc. Income	-	-	24/-
Insurance	58,420/-	50,468/-	1,23,330/-	Interest received	-	29,847/-	-
Printing & stationery	6,283/-	18,819/-	5,412/-	Rent received	2,22,70,851/-	-	-
Staff Welfare Expenses	29,194/-	29,909/-	42,198/-	Credit balances written back	15,767/-	-	-
Security services	1,13,166/-	1,03,782/-	1,15,812/-				
Postage & telephones	23,132/-	24,228/-	17,056/-				
Legal & professional charges	4,53,223/-	75,341/-	59,857/-				
House tax paid	82,427/-	-	21,601/-				
Commission paid	20,594/-	21,039/-	69,602/-				
Bad debts	-	2,79,487/-	-				
Repair & maintenance	3,95,354/-	19,750/-	31,643/-				
Interest & bank charges	61,45,302/-	85,21,032/-	84,29,737/-				
Employer's contribution towards provident fund & ESI	22,024/-	25,544/-	25,869/-				

From the above details, it is clear that the assessee's turnover is continuously going down. The closing stock is also decreasing in the year 2006-07 and there is minor increase in the year 2007-08 and 2008-09. The financial results of the business activities undertaken by the assessee are very poor. The assessee has credited rental income in the profit and loss account, therefore, it is resulting into profit in the F.Y. 2008-09. From the examination of balance sheet, incorporated in the assessment order and the appellate order, we find that the assessee has taken loan from Punjab National Bank, which are continuously

decreasing. This shows that the assessee is making payment to the bank. The balance sheet further shows that the capital account of the partners is showing continuous debit balances. It seems that the partners have drawn excess money from the firm which is resulting into debit of the partner's capital account. In view of these facts the findings of the Id. Assessing Authority noted above cannot be straightway side tracked. A perusal of the impugned order reveals that the Id. CIT(A) has deleted the addition only on the ground that such expenses were allowed in the preceding assessment years 2002-03 to 2006-07 on the identical facts. The record nowhere reveals whether the loan taken by the assessee was a term loan for construction/renovation etc. of building, or it was working capital loan taken for the purpose of business. No documentary evidences of the bank are available before us to ascertain this fact. Secondly, the Id. CIT(A) has failed to consider the new fact emerged only in the year under consideration, inasmuch as three floors of the building are let out by the assessee and remaining two floors were used for business purposes. Therefore, in case, it was a term loan taken for construction/renovation of building, then the expenses incurred by the assessee on such loan, shall be apportioned in the ratio of 60:40 as done in the case of other expenses dealt by the Id. CIT(A) itself. If it was a working capital loan, then it has to be thrashed out as to under what circumstances and for

what purpose, the capital accounts of the partners were showing continuous debit balances. All these facts need verification at the stage of Assessing Officer before finally deciding the issue. We, therefore, think it appropriate to remand the issue to the file of Assessing Officer to decide the same afresh after making thorough enquiry in the light of observations made above and by way of speaking order. Needless to say, the assessee shall be given reasonable opportunity of being heard. Accordingly, grounds Nos. 6 & 7 of the Revenue's appeal are allowed for statistical purposes.

18. The next and last ground No.8 challenges the deletion of addition of Rs.26,00,000/- made u/s. 68 of the Act. In the assessment proceedings on perusal of the balance sheet of the assessee, the AO noticed that the assessee had shown a loan of Rs.26,00,000/- from one Sh. Rajendra J. Hinduja, in support of which the assessee filed two letters of the creditors, which were the covering letters of the creditor for sending the DDs of the above amount. The above letters not being in the nature of confirmation of creditors giving details of nature of transaction, the AO required the assessee to file the original confirmation of the creditor of advancing loan to the assessee alongwith bank statement, IT return, PAN etc. However, by the time the original confirmation was alleged to have been placed before the AO, the assessment order is said to

have been passed. The Assessee, therefore, sent these documents by speed post to the AO and also furnished the same before the Id. CIT(A) alongwith application for admitting additional evidences, which stood admitted after giving proper opportunity to the AO. The AO also furnished remand report on the issue after enquiry. The AO disallowed the claim of assessee as the creditworthiness of creditor and genuineness of the transaction stood unproved before him. The Id. CIT(A) considering the evidences furnished deleted the addition holding that the lender was the old creditor of the assessee and all the ingredients of section 68 stood satisfied.

19. We have considered the rival submissions on the issue and we find no justification to interfere with the order of the Id. CIT(A). It is notable that the lender is an old creditor, as he had an opening balance and his PAN was already available on record. During the enquiry made by AO in the remand proceedings, the creditor had satisfied the requirements of the AO. The copy of IT return of the creditor filed showing total income at Rs.93,02,056/- in our opinion, goes to prove the creditworthiness of the creditor as also observed by Id. CIT(A). Considering all these facts, we are of the considered opinion that the Id. CIT(A) has rightly deleted this addition u/s. 68 of the Act. No good case

is made out on behalf of the Revenue to support the assessment order on this count. Accordingly, ground No. 8 of the Revenue's appeal stands dismissed.

20. In the result, the appeal of the Revenue is partly allowed for statistical purposes.

Order pronounced in the open court on 30-10-2015.

Sd/-

(H.S. SIDHU)
Judicial Member

Sd/-

(L.P. SAHU)
Accountant Member

Dated :
*aks/-

Copy of order forwarded to:

(1) *The appellant*
(3) *Commissioner*
(5) *Departmental Representative*

(2) *The respondent*
(4) *CIT(A)*
(6) *Guard File*

By order

Assistant Registrar
Income Tax Appellate Tribunal
Delhi Benches, New Delhi