

**IN THE INCOME TAX APPELLATE TRIBUNAL
ALLAHABAD ‘SMC’ BENCH, ALLAHABAD**

(THROUGH VIRTUAL COURT),

BEFORE SHRI.VIJAY PAL RAO, JUDICIAL MEMBER

**ITA No.322/ALLD/2017
Assessment Year: 2010-11**

M/s Universal Stone Crushing Co. Dala, Sonebhadra- 231207 PAN-AABFU7845A	v.	Income Tax Officer, Range-3(3), Mirzapur
(Appellant)		(Respondent)

Appellant by:	Shri O.P. Shukla, Advocate
Respondent by:	Mr. A.K. Singh, Sr. DR
Date of hearing:	22.06.2021
Date of pronouncement:	24.06.2021

ORDER

This appeal by the assessee is directed against the order dated 20.09.2017 of CIT(A) for the assessment year 2010-11. The assessee has raised the following grounds:-

- “1. Because, the Ld. commissioner of income tax (A) Allahabad was not justified to conform the order of the assessing officer by charging interest u/s 40(b)(iv) at Rs.29529.00 on the pro-rata basis.*
- 2. Because the learned Commissioner of Income Tax (Appeal) Allahabad was not justified to conform the adhoc disallowance a sum of Rs.53280/- under the head repair and maintenance out of the total exps debited to the P&L a/c.at Rs 1065600/-.*
- 3. Because the learned Commissioner of Income Tax (Appeal) Allahabad was not justified to conform the addition made by the assessing officer a sum of Rs 50000/- under the head valuation of closing stock of dust of grits on the basis of adhoc disallowances.*

4. *Because the learned Commissioner of Income Tax (Appeal) Allahabad was not justified to conform the adhoc disallowance a sum of Rs 6066/- under the head interest paid on VAT.*
5. *Because the learned Commissioner of Income Tax (Appeal) Allahabad was not justified to conform the adhoc disallowance sum of Rs 9980/- under the] customer entertainment exps out of the total amount debited to the P & L a/c of Rs 49900/-.*
6. *Because the learned Commissioner of Income Tax (Appeal) Allahabad was not justified to conform the adhoc disallowance a sum of Rs 5668/- under the head telephone exps out of the total amount debited to the P& L A/c Rs 28340/-.*
7. *Because the appellant case is covered by the several judgment of Hon'ble ITAT in case of Chandra Confectionery Pvt. Ltd. 2003(2) MTC 1022, whether the court held that no any disallowance can be made on lump- sump basis otherwise any specific defect found in the books of accounts.*
8. *Because, the appellant craves for a right to raise any additional ground during the course of hearing of the case.*
9. *Because the order passed by the Ld. Commissioner (Appeal) is erroneous, bad in law and on facts and against the judgment jurisdictional court and is deserve to be quashed."*

2. Ground No.1 is regarding restriction of claim of interest payment on partner's capital. The assessee is a partnership firm and claimed interest of Rs.1,04,734/- on opening balance of partner's capital @ 12% per annum. During the assessment proceedings, the Assessing Officer noted that the assessee has paid the interest on the opening balance of Rs.8,72,785/- but during the year Shri Satish Kumar Agarwal, the partner of assessee firm has drawn Rs.8,55,587/- and consequently, the closing balance in the capital account of Shri Satish Kumar Agarwal is Rs.3,80,600/-. The Assessing Officer was of the view that the allowable interest on the opening balance for the full year is not admissible due to substantial withdrawal by the partner. Accordingly, the Assessing Officer allowed the interest on account of partner's capital on pro rata basis i.e. by taking average of the opening balance and closing balance. Accordingly, the Assessing Officer allowed the interest on partner's capital of

Rs.29,529/- as against the claim of Rs.1,04,734/-. The assessee challenged the action of the Assessing Officer before the CIT(A) but could not succeed.

3. Before the Tribunal, the ld. AR has submitted that the assessee firm has made the payment of interest to the partner Shri Satish Kumar Agarwal of Rs.1,04,734/-. The said payment is based as per the terms of partnership deed which provides the interest on the partner's capital on the opening balance. Therefore, the ld. AR has contended that when the assessee has made the payment of interest on the partner's capital as per the terms of the partnership deed then in view of Section 40(b)(iv) of the Income Tax Act, 1961 (in short the 'Act') the interest on the opening balance of the partnership capital @ 12% is allowable claim. Hence, the ld. AR has contended that the Assessing Officer is not justified in making the disallowance by applying the pro rata basis while considering the claim of interest paid to the partner.

4. On the other hand, ld. DR has submitted that Section 40(b)(iv) of the Act is not a provision to allow the claim of interest on partner's capital but it lays down certain extra conditions to be satisfied for allowing the deduction on account of interest paid to the partner. Thus, the ld. DR has submitted that allowability of claim has to be considered under Section 36(1)(iii) or Section 37 of the Act. Once the capital was not with the partnership firm during the year under consideration then the interest for the entire year on the opening balance is not allowable as per the provisions of Section 36(1) as well as Section 37 of the Act. He has relied upon the orders of the authorities below.

5. I have considered the rival submissions as well as relevant material available on record. The dispute is about the allowability of the interest paid to the partner by the assessee firm calculating on the opening balance of the capital account of the partner without considering the subsequent withdrawals made by the partner. The assessee has taken a stand that since the partnership deed provides the payment of interest on the opening balance of the capital account of the partner, therefore, the

subsequent withdrawals of the amount from the capital account of the partner is irrelevant. It is pertinent to note that Section 40(b)(iv) is restrictive in nature and not a provision enabling the deduction. For the ready reference Section 40(b)(iv) is reproduced as under:-

“Amounts not deductible.

40. Notwithstanding anything to the contrary in sections 30 to 38, the following amounts shall not be deducted in computing the income chargeable under the head "Profits and gains of business or profession".

(a) xxxxxxxxxxxxxxxxx

(b) in the case of any firm assessable as such,-

(i) to (iii) xxxxxxxxxxxxx

(iv) any payment of interest to any partner which is authorised by, and is in accordance with, the terms of the partnership deed and relates to any period falling after the date of such partnership deed in so far as such amount exceeds the amount calculated at the rate of twelve per cent simple interest per annum; or”

6. Thus the plain reading of Section 40 itself shows that this provision begins with a non obstante clause meaning thereby certain amounts are not deductible even if the same are allowable u/s. 30 to 38 of the Act. Therefore, the provisions of Section 40 cannot be invoked directly for allowing the claim but the claim of deduction has to be first tested in terms of Sections 30 to 38 of the Act, and once the claim is allowable under the provisions of Sections 30 to 38 of the Act then certain amounts as specified u/s. 40 are allowed as deduction only on satisfaction of specified conditions provided under this section. Thus, it is discernable that section 40 is a restrictive section which imposes further condition for allowing the certain deduction against business income. Clause (b) of Section 40 pertains to claim of deduction by a partnership firm and sub clause (iv) contemplates certain conditions in respect of the payment of interest to any partner which is authorized and by in accordance with the terms of

partnership deed. This sub clause also provides the outer limit of rate of interest being 12% simple interest per annum. Hence, the provisions of Section 40(b) can be invoked only to verify whether the claim of interest paid to the partner is in accordance with the terms of the partnership deed and the maximum allowable rate is 12% simple interest per annum. Prior to invoking the section 40 of the Act the claim has to satisfy the conditions as provided u/s. 30 to 38 of the Act and in case in hand the interest paid to the partner has to be first allowable under the provisions of Section 36(1)(iii) or Section 37(1) of the Act. Both these provisions i.e. Section 36(1)(iii) as well as Section 37 stipulates a mandatory condition that the expenditure has been laid out for the purpose of business of the assessee. The residual provision of Section 37(1) rather prescribes more stringent condition that an expenditure has been laid out wholly and exclusively for the purpose of business or profession. Thus, for allowing the claim of interest paid to the partner it has to be first considered in terms of Section 36(1)(iii) or the section 37(1) of the Act and then the claim has to be restricted as per the provisions of section 40(b)(iv) of the Act.

7. In the case in hand, there is no dispute that the opening balance in the capital account of the partner, Shri Satish Kumar Agarwal was Rs.8,72,785/- but during the year the said partner has withdrawn a sum of Rs.8,55,587/- which means the substantial amount except a meager sum of Rs.3,80,630/- was withdrawn by the partner and was not available with the partnership firm for its business purpose. Hence, the claim of interest for full year @ 12% is otherwise not allowable in terms of Section 36(1)(iii) or Section 37(1) of the Act as the case may be. Once the basic condition as prescribed u/s 36(1) (iii) or Section 37(1) of the Act was not satisfied regarding allowability of particular claim of interest then the said claim cannot be allowed by invoking the Section 40(b)(iv) of the Act, which is a restrictive provisions and not enabling provision. Accordingly, the Assessing Officer has rightly allowed the claim on pro-rata basis i.e. the average of opening and closing balance was taken as

eligible amount while allowing the interest paid to the partner. This ground of the assessee's appeal is dismissed.

8. Ground no. 2 is regarding disallowance of 5% of repair and maintenance expenditure. The Assessing Officer asked the assessee to explain the details of TDS payment on transport expenses. In response, the assessee submitted that the assessee has utilized number of trucks and no TDS was deducted in respect of the payment made as not exceeding Rs.50,000/- to each trucks. The Assessing Officer further noted that the repairs and maintenance expenses debited by the assessee to the tune of Rs.10,65,600/- are not fully verifiable. Accordingly, the Assessing Officer made an adhoc disallowance of 5% which comes to Rs.53,280/-. The assessee challenged the action of the Assessing Officer before the CIT(A) but could not succeed.

9. Before the Tribunal, the Id. AR of the assessee has submitted that the expenditure incurred on account of the repair and maintenance are recorded in the books of account which are fully audited by the chartered accountant. During the course of assessment proceedings, the assessee produced complete books of account, bills and vouchers. The Assessing Officer accepted the book result and therefore, the adhoc disallowance made by the Assessing Officer in respect of the repair and maintenance expenses is not justified. He has referred to the ledger account of repair and maintenance and submitted that the assessee has fully accounted all these expenses. In support of his contention he has relied upon the decision of Hon'ble jurisdictional High Court in the case of CIT vs. Babu Ram Ajit Prasad, 106 ITR 818. He has also referred various decisions of this Tribunal on the point of adhoc disallowance made by the Assessing Officer. The Id. AR has submitted that the disallowance made by the Assessing Officer may be deleted.

10. On the other hand, Id. DR has submitted that the Assessing Officer has given a finding that the claim of expenditure under the head repair and maintenance has not been substantiated by the assessee by producing verifiable vouchers and others

evidence. The entire payment claimed to have been made in cash. Therefore, in the absence of necessary details and supporting documentary evidence the Assessing Officer is justified in disallowing 5% of these expenses. In support of his contention, he has relied upon the decision of the Hon'ble jurisdictional High Court in the case of Pr. CIT vs. Rimjhim Ispat Ltd., 382 ITR 152. He has also relied upon the orders of the authorities below.

11. I have considered the rival submissions as well as relevant material available on record. The assessee has claimed a sum of Rs.10,65,600/- under the head repair and maintenance. The Assessing Officer has stated in the assessment order that the claim of the assessee is not verifiable and accordingly the Assessing Officer made disallowance of 5% of such expenses which comes to Rs.53,280/-. The CIT(A) has confirmed the disallowance made by the Assessing Officer by recording the reasons that the assessee has not produced any record in support of the claim. There is no quarrel on the point that if the claim of expenditure is found to be genuine and incurred for the purpose of business of the assessee then without giving a finding that a specific amount is not incurred towards the purpose of business of assessee the Assessing Officer ought not to have made an adhoc disallowance. However, in the case in hand, the assessee has claimed Rs.10,65,600/- under the head repair and maintenance and all these expenditure are claimed to have been incurred in cash. The copy of ledger accounts of plant repair and maintenance is placed at pages 14 to 18 of the paper book. Ongoing through the details and entries of the ledger account it is noted that the assessee has shown the entries of the expenditure throughout the year for less than twenty thousand of each payments. Except the narration of being cash paid for plant repair and maintenance no other particulars or details are mentioned in the ledger account. Even the vouchers claimed by the assessee are not produced before the Tribunal and the same are claimed as self-made vouchers. Since the assessee has not produced the vouchers, therefore, the only inference can be drawn from ledger account of the repair and maintenance expenses is that these expenses

are not substantiated by the assessee by producing a verifiable supporting documentary evidence. The nature of payment being each less than 20,000/- shows that the assessee has carried out the entries to avoid the TDS provisions. Since all the payments are made in cash and no details are provided by the assessee to whom the payments are made therefore, the assessee has failed to prove that the claim of expenditure incurred by the assessee on account of repair and maintenance is a genuine claim. Accordingly, in the facts and circumstances of the case 5% disallowance made by the Assessing Officer is found to be reasonable and justified. The Hon'ble jurisdictional High Court in the case of Pr. CIT vs. Rimjhim Ispat Ltd. (Supra) has held in paras 7 and 8 as under:

"7. Having heard the learned counsel for the parties, we find that there is an express finding given by the Assessing Authority as well as by the Ist Appellate Authority with regard to non-production of bills and vouchers and for not maintaining the stock register. In the absence of non-production of bills and vouchers, the Assessing Officer was justified in disallowing certain expenditure by 10%, which was reduced by the Ist Appellate Authority to 5%. This aspect had not at all been considered by the Tribunal and the same had only been allowed on the ground that the turnover has increased by 5% and the expenditure has reduced. The Tribunal has lost sight of the fact that the expenditure claimed under the head manufacturing expenses, which forms part of the "profit and loss account", showing expenses made by the assessee are required to be proved by production of bills and vouchers. In the absence of production of bills and vouchers, an inference can be drawn by the Assessing Authority that such expenses shown under this head were inflated or were not supported by any bills, vouchers or any other documentary evidence, which would justify the Assessing Officer in disallowing certain portion of such expenses.

8. In the light of the aforesaid, we are of the opinion that the Tribunal committed an error in allowing the appeal of the assessee and by totally deleting the disallowance of 5%. We, accordingly, allow the Ist question of law as stated aforesaid, in favour of the appellant, i.e., the Department and against the assessee and set aside that part of the order of the Tribunal on this aspect and restore the order of the Ist Appellate Authority. In our opinion, the disallowance of 5% in the facts of the case is justified."

12. The decision relied upon by the AR of the assessee in the case of CIT vs. Baburam Ajit Prasad (Supra) would not help the case of the assessee. The said decision is only in respect of a possible view and opinion and the Assessing Officer

taken a view against the assessee. Accordingly, this ground of the assessee's appeal is dismissed.

13. Ground No.3 is regarding the addition made by the Assessing Officer on account of valuation of closing stock of dust. The assessee has valued the closing stock of dust at Rs.1,90,200/-. The Assessing Officer asked the assessee about the maintenance of the quantitative stock and stock register. The assessee explained that there is no stock of grit but the closing stock is only in respect of the dust which is a scrap/residual generated during the manufacturing of grit. The Assessing Officer accordingly made an adhoc addition of Rs.50,000/- to be closing stock of the assessee and consequently added to the income of the assessee. The assessee challenged the action of the Assessing Officer before the CIT(A) but could not succeed.

14. Before the Tribunal, the ld. AR of the assessee has submitted that the assessee has shown stock of dust generated out of stone chip to the tune of Rs.1,90,200/-. The Assessing Officer has made an adhoc addition without any basis on the ground that the assessee is not maintaining quantitative details and stock register. He has further submitted that only the stock of stone chips/grit is required to be maintained as finished goods but the dust generated during the course of manufacturing is only scrap in nature and not required to be quantified. The assessee has value the stock of stone chip/dust on lump-sum basis of Rs.1,90,200/-. The ld. AR has submitted that adhoc addition made by the Assessing Officer to the closing stock of the assessee is not justified.

15. On the other hand, the ld. DR has submitted that the assessee has not produced the Annexure No.IV to the balance sheet though the same is mentioned in the audit report in column No. 28(b). The assessee has not furnished any record to justified the valuation of the closing stock of Rs.1,90,200/-. Hence, the Assessing Officer is justified in making the reasonable addition of Rs.50,000/-. He has relied upon the orders of the authorities below.

16. I have considered the rival submissions and relevant material available on record. There is no dispute that the assessee has not maintained the quantitative details of the stock of dust of stone chips but the closing stock is value at lump-sum of Rs.1,90,200/-. The Assessing Officer in the assessment order has made an adhoc addition of Rs.50,000/- to the closing stock of dust without even considering the volume or any other parameters for such adhoc valuation. Even the Assessing Officer has not tried to estimate by wild guess work but the addition is purely on adhoc addition without any reasonable basis. Once the Assessing Officer is not satisfied about the valuation of the closing stock of the dust then it is incumbent upon the Assessing Officer to conduct a proper enquiry and to apply proper criteria or basis for valuation of the closing stock. The wrong valuation of the closing stock on the part of the assessee does not authorize the Assessing Officer to make a wrong addition. Therefore, even if the valuation of the closing stock made by the assessee is not found to be correct the Assessing Officer has to make the valuation on some proper guidance and criteria. In the absence of any basis the adhoc addition made by the Assessing Officer is not justified and the same is deleted. It is pertinent to note that since the closing stock shown by the assessee is regarding the dust of the stone chip which is generated during the course of the manufacturing of the stone chip. Therefore, the assessee has explained the reasons for not maintaining the quantitative details and maintaining the stock register of such dust stock. Once the explanation of the assessee is reasonable keeping in view the nature of scrap generating during the manufacturing process then the action of the Assessing Officer in making the adhoc addition is not justified. Hence, the addition made by the Assessing Officer is deleted.

17. Ground No.4 is regarding addition under the head interest paid on VAT of Rs.6066/-. At the time of hearing, the Id. AR of the assessee has stated at bar that the assessee does not press this ground and the same may be dismissed as not pressed.

18. Ld. DR has no objection if Ground No.4 of the appeal is dismissed as not pressed. Accordingly, the Ground No. 4 of the assessee's appeal is dismissed being not pressed.

19. Ground No.5 is regarding disallowance of entertainment expenses @ 20%. The assessee has claimed Rs.49,900/- as customer entertainment expenses. The Assessing Officer noted that the expenses are not verifiable therefore, he disallowed 1/5th of the expenditure to the tune of Rs.9,980/-. The assessee challenged the action of the Assessing Officer before the CIT(A) but could not succeed.

20. Before the Tribunal, the ld. AR has submitted that the expenditure incurred in entertainment of the customer is a petty expenditure incurred in cash and there cannot be any proper voucher in respect of such type of expenditure. Therefore, an adhoc disallowance made by the Assessing Officer is not justified.

21. On the other hand, ld. DR has relied upon the orders of the authorities below.

22. Having considered the rival submissions as well as relevant material on record. It is noted that the Assessing Officer has made disallowance of 20% of the entertainment expenses on the ground of not fully verifiable. The Assessing Officer made a similar disallowance in respect of the repair and maintenance expenses but @ 5% which has been confirmed by this Tribunal in the preceding part of this order. Accordingly to maintain the rule of consistency the disallowance made by the Assessing Officer is restricted to 5%. This ground of the appeal is partly allowed.

23. Ground No.6 is regarding disallowance of telephone expenses, the Assessing Officer has made disallowance @ 20% of telephone expenses on the ground of personal use of partners.

24. I have heard the rival submissions and considered the relevant material on record. The Assessing Officer made the disallowance on the ground of personal use in respect of telephone expenses. However, the Assessing Officer has not discussed

anything about the personal use of telephone. Hence, except the suspicion of the Assessing Officer regarding the possible personal use of telephone by the partners nothing has been brought on record by the Assessing Officer to substantiate such suspicion of personal use. Further, since the telephone expenses are fully verifiable and supported by the bills and other details therefore, once the assessee has claimed the telephone expenses based on actual payment/due then the disallowance on the ground of personal use cannot be allowed without bringing some tangible material or facts on record. Accordingly, the disallowance made by the Assessing Officer on account of telephone expenses is not justified, the same is deleted.

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

Order pronounced in the open Court on 24.06.2021 through video conferencing.

Sd/-
[VIJAY PAL RAO]
JUDICIAL MEMBER

DATED: 24/06/2021
Aks/-

Copy forwarded to:

1. Appellant –
2. Respondent –
3. CIT(A) , Allahabad
4. CIT
5. DR -

By order
Assistant Registrar

		Date	Initials	
	Original dictation pad is enclosed at the end of file			
1.	Draft dictated on:	22.06.2021		Sr. PS/PS
2.	Draft placed before author:	23.06.2021		Sr. PS/PS
3.	Draft proposed & placed before the second member:			JM/AM
4.	Draft discussed/approved by Second Member:			JM/AM
5.	Approved Draft comes to the Sr. PS/PS:	23.06.2021		Sr. PS/PS
6.	Order pronounced on:	24.06.2021		Sr. PS/PS
7.	File sent to the Bench Clerk:	24p.06.2021		
8.	Date on which file goes to the Head Clerk:			Sr. PS/PS
9.	Date on which file goes to AR			
10.	Date of dispatch of Order:			