

2011-TIOL-538-ITAT-KOL

**IN THE INCOME TAX APPELLATE TRIBUNAL
BENCH 'C' KOLKATA**

**ITA Nos.554 & 555/Kol/2011
Assessment Years: 2006-07 & 2007-08**

**DEPUTY COMMISSIONER OF INCOME TAX
CC-XIII, KOLKATA**

Vs

**M/s HALDIRAM BHUJIAWALA LIMITED, KOLKATA
PAN NO:AAACH6301A**

S V Mehrotra, AM and Mahavir Singh, JM

Dated: July 28, 2011

**Appellant Rep by: Shri D J Mehta
Respondent Rep by: Shri S M Surana**

Income tax – Sections 37, 40A(2), 145(3) – Whether when the books of account of the assessee are rejected and assessee has not appealed against the same, the GP rate is to be estimated only on reasonable basis – Whether the foreign travelling expenses incurred on director of the company for setting up a subsidiary abroad is allowable as it has a direct nexus with business – Whether the commission paid to ‘K’ can be disallowed u/s 40A(2)(a) without considering whether it was excessive or unreasonable having regard to the fair market value of the services rendered by the person.

A) Assessee-company was engaged in manufacturing and distribution of processed food and beverage. AO noticed that G.P. rate in AY 2005-06 was 15.87% whereas it was 14.28% in AY 2006-07. Assessee explained that it was due to massive increase in the price of Cooking Gas which was increased by 74.21%. AO found that assessee did not maintain any stock register for purchase, production and consumption. The opening and closing stock was certified by the assessee. Assessee also failed to produce relevant vouchers, bills/invoices in support of cash purchases of milk, which is one of the essential ingredients of the trade. Assessee only produced computerized ledger of sales without any cash or other evidences. He rejected the assessee's contention that it was not possible in this business to issue cash memo for every routine and small retail sales. Thus the provisions of Section 145(3) were invoked doubting the correctness and completeness of the accounts of the assessee and rejected the manufacturing and trading results shown by the assessee and made addition by applying higher GP rate. CIT (A) confirmed the findings of the Assessing Officer in regard to rejection of books of account however deleted the addition observing that AO did not bring any evidence to prove any sales outside the books of account and assessee's explanation for fall in GP rate had not been rebutted by the AO.

In appeal, the assessee contended that it had filed audited accounts containing all the

quantitative details. In the assessment orders for A.Y. 2004-05 and 2008-09, no addition had been made either in earlier year or in subsequent years. Tax Audit Report demonstrated break-up of raw material consumed, value of imported and indigenous raw material consumed, quantitative details relating to goods manufactured/traded and licensed capacity/installed capacity of goods manufactured.

B) Assessee debited travelling expenses of foreign travel undertaken by director of the company to London. Assessee contended that the company had been intended to set up a wholly owned subsidiary at the United Kingdom, for marketing and distribution of its range of Food Products. The proposed name of the subsidiary company is "Haldiram clay oven U.K. Ltd." The Directors had visited the U.K. for negotiating an office / Showroom for the above business. Further, the expenses had been covered by FBT. AO disallowed the expenses stating that assessee could not furnish any evidence to demonstrate that new avenue for the activity of the company was explored neither for the year of travel nor for the subsequent year. Assessee failed to substantiate the nexus of the foreign travel expenses vis-a-vis the business expenditure. CIT (A) allowed the appeal of the assessee.

C) Assessee incurred commission to Smt. 'K'. AO asked the assessee to explain the services rendered by 'K'. Assessee contended that it was paid @ 1% on turn over achieved from an outlet at Kolkata. The amount was paid to her in lieu of services the company was taking for its benefit and growth. Further AO observed that no service could be rendered by a lady aged more than 70 years of age. Ld. CIT(A) allowed the appeal observing that in the assessment of Smt. 'K', the commission had been taxed. The responsibility of growth and profitability of a particular retail outlet of assessee-company had been assigned to Smt. 'K'.

After hearing both the parties, the ITAT held that,

A) ++ CIT(A) confirmed the findings of the Assessing Officer on the issue of rejection of the books of account and the assessee is not aggrieved by the said findings. The issue remains for consideration is how to estimate the assessee's income. AO is required to estimate the assessee's income on a reasonable basis having regard to all the details available with him. As far as the sales returned by the assessee is concerned, same could not be disturbed in the absence of any evidence to show that there was some sales outside the books of account. Mere non-issuance of cash memos for every routine and small details of sales could not be the basis for rejection of turnover returned by the assessee;

++ since the assessee's book results had been rejected, therefore, it has to be examined as to what extent assessee's G.P. rate of 14.287% could be accepted. The assessee had given an explanation in regard to increase in the price of Cooking Gas which has not yet been rebutted by the AO. The other main reason for rejection of books of account was that assessee failed to produce relevant vouchers/bills, invoices in support of cash purchases of milk. AO has rightly observed that onus is on the assessee to prove its claim of expenditure. Under such circumstances, it would meet the ends of justice if G.P. rate is estimated at 14.5% as against 15.08% determined by Assessing Officer. Thus, this ground of the Department is partly allowed;

B) ++ assessee had shown export turn over of Rs.1.00 crores to UK. Therefore, assessee's claim regarding visit of Director to UK for business purposes cannot be doubted. The assessee had produced all the relevant correspondence in this regard which has been taken note of by CIT(A) and not rebutted by Department. Therefore, the appeal of the revenue is dismissed;

C) ++ the commission had been paid to mother of Director of assessee-company who had been associated with this business for considerable long time. Commission has been paid for the last 25 years and the lady still manages the outlet. Merely her age being 70 years, cannot be a basis for making disallowance. Her presence itself in the outlet was more than sufficient for making the payment of commission to her as she could manage the affairs effectively merely by sitting at the outlet. AO made disallowance by referring to Section 40A(2)(a), but he has not made disallowance on the ground of the same of being excessive and unreasonable. Disallowance was made observing that it was an accommodation of expenses paid to a person satisfied u/s. 40A(2)(a). AO has wrongly referred to Section 40A(2)(a) because u/s. 40A(2)(a), disallowance can be made if the expenditure is considered to be excessive and unreasonable having regard to the fair market value of the services rendered by the person. Thus, the order of CIT (A) is confirmed.

Revenue's appeal partly allowed

ORDER

Per: S V Mehrotra:

The Department has filed these two appeals against order of Ld. CIT(A), Central-II, Kolkata for assessment years 2006-07 & 2007-08. All these appeals were heard together and are being disposed of by this common order for the sake of convenience.

2. The grounds are common in all the three appeals and, therefore, for the sake of convenience, we refer to the facts as obtaining in assessment year 2006-07 vide ITA No.554/Kol/2011.

3. The first ground taken by the Department is as under :-

"That in the facts and circumstances of the case and in law, the Ld. CIT(A) has erred in deleting the addition of Rs.30,78,972/- made on account of low gross profit while holding that assessee had accepted the rejection of books of accounts and without appreciating the materials brought on record and facts evaluated by the AO in the assessment order."

4. Brief facts of the case are that the assessee-company in the relevant assessment year was engaged in manufacturing and distribution of processed food and beverage. It had filed its return of income declaring total income of Rs.1,05,69,200/-. The Assessing Officer noticed that G.P. rate in assessment year 2005-06 was 15.87% whereas it was 14.28% in assessment year 2006-07. The assessee explained that the fall in G.P. rate of 1.59% was due to massive increase in the price of Cooking Gas which was increased by 74.21% during the intervening period from 01.04.2004 to 31.03.2006. The Assessing Officer examined the assessee's accounts and found that assessee did not maintain any stock register for purchase. There was no record for the production and consumption either. The opening and closing stock was certified by the assessee. He further observed that assessee failed to produce relevant vouchers, bills/invoices in support of cash purchases of milk, one of the essential ingredients of the trade, amounting to Rs.45,95,508/- during the year. The assessee had only produced the details of journal entries in respect of cash purchases. As regards the sales, Assessing Officer observed that assessee had produced computerized ledger of sales without any cash or other evidences. He did not accept the assessee's contention that it was not possible in this business to issue cash memo for

every routine and small retail sales. He, therefore, concluded that sales shown at Rs.30,56,54,251/- during the year was not verifiable. In view of these discrepancies, he invoked the provisions of Section 145(3) doubting the correctness and completeness of the accounts of the assessee and rejected the manufacturing and trading results shown by the assessee. He estimated the sales at Rs.31.00 crores and applied the average G.P. rate of 15.08% being average of [14.287% + 15.879%] on the net turn over of Rs.31.00 crores. He, accordingly, made an addition of Rs.30,78,972/-. The Ld. CIT(A) after considering the assessee's submission confirmed the findings of the Assessing Officer in regard to rejection of books of account. However, he deleted the additions for the following reasons :-

(i) Assessing Officer did not bring any evidence to prove any sales outside the books of account and, therefore, the sales as returned by the assessee at Rs.30,56,54,251/- could not be disturbed.

(ii) Assessee's explanation for fall in G.P. rate as compared to assessment year 2005-06 had not been rebutted by the Assessing Officer. Therefore, the rate of 14.28% [wrongly mentioned by Ld. CIT(A) 14.49%] returned by the assessee could not be disturbed as assessee has shown reasonable profit.

5. Ld. Departmental Representative submitted that Assessing Officer was quite reasonable in making a very miniscule addition of Rs.30,78,972/- by increasing the G.P. rate because the books were rejected by the Assessing Officer and also confirmed by the Ld. CIT(A).

6. Ld. Counsel appearing on behalf of the assessee submitted that assessee had field audited accounts containing all the quantitative details. He filed before us, assessment order for assessment year 2004-05 and assessment year 2008-09, pointing out that no addition had been made either in earlier year or in subsequent years. He has also filed extracts from Tax Audit Report to demonstrate that the following details were furnished by the assessee :-

- (a) Break-up of raw material consumed;
- (b) Value of imported and indigenous raw material consumed.;
- (c) Quantitative details relating to goods manufactured/traded;
- (d) Licensed capacity/installed capacity of goods manufactured.

Ld. Counsel relied on the decision in the case of *ITO vs. TEXCO INDIA 1996-(055)-TTJ-TDEL*, wherein under similar circumstances Tribunal had upheld the Ld. CIT(A)'s finding in deleting the addition.

7. We have considered the submissions of both the parties and have perused the records of the case. The assessee's books were rejected for the various reasons given by the Assessing Officer as noted earlier. The Ld. CIT(A) confirmed the findings of the Assessing Officer on this issue and the assessee is not aggrieved by the said findings. Now, the issue which remains for consideration is how to estimate the assessee's income. It is well settled law that the Assessing Officer is required to estimate the assessee's income on a reasonable basis having regard to all the details available with him. In this regard, we find that as far as the sales returned by the assessee is concerned, same could not be

disturbed in the absence of any evidence to show that there was some sales outside the books of account. The assessee had maintained its sales on computer and, therefore, mere non-issuance of cash memos for every routine and small details of sales could not be the basis for rejection of turn over returned by the assessee. We find ourselves in complete agreement on this count with the Ld. CIT(A).

7.1 Now, coming to the G.P. rate of 15.08% applied by the Assessing Officer as against 14.28% returned by the assessee, we are of the opinion that since the assessee's book results had been rejected, therefore, it has to be examined as to what extent assessee's G.P. rate of 14.287% could be accepted. The assessee had given an explanation in regard to increase in the price of Cooking Gas which has not yet been rebutted by the Assessing Officer. The other main reason assigned by the Assessing Officer for rejection of books of account that assessee had failed to produce relevant vouchers/bills, invoices in support of cash purchases of milk. The Assessing Officer has rightly observed that onus is on the assessee to prove its claim of expenditure. Hon'ble Supreme Court in the case of *CIT vs. Calcutta Agency Limited [1951] 19 ITR 191 (SC)* has held that onus lies on the assessee to establish its claim. Under such circumstances, we are of the opinion that it would meet the ends of justice if G.P. rate is estimated at 14.5% as against 15.08% determined by Assessing Officer. We direct, accordingly. This ground of the Department is partly allowed.

8. Ground No.2 reads as under :-

"That in the facts and circumstances of the case and in law, the Ld. CIT(A) has erred in deleting the addition of Rs.13,08,979/- made on account of foreign travel of the Director without appreciating that disallowance was made on account of non-business expenditure of the assessee as the assessee had failed to establish any business connection with the foreign trips."

9. Brief facts apropos this ground are that assessee had debited Rs.23,48,860/- as travelling expenses to the profit & loss account which included foreign travel expenses of Rs.16,36,223/- undertaken by Shri Prabhu Shankar Agarwal, Director of the Company to London during the year. The assessee had filed following explanation :-

"It was explained and submitted in the course of assessment proceedings for the A. Y. 2004-05 that the company had been intended to set up a wholly owned subsidiary at the United Kingdom, for marketing and distribution of its range of Food Products. The proposed name of the subsidiary company is "Haldiram clay oven U.K. Ltd." During the period 06.04.2003 to 19.04.2003 the Directors had visited the U.K. for negotiating an office / Showroom for the above business. A letter dated 23.05.2003 sent by Speed Post to the Hon'ble Indian High Commissioner in the above matter is enclosed herewith again for your perusal. The current visit is also in continuation and in the chase of the above purpose."

Further we like to in form you that the expenses Rs.16,36,223/- made on account of the Foreign Travel has been covered by FBT and the due FBT has been paid by us"

The Assessing Officer observed that assessee had only furnished photo-copy of the letter addressed to Hon'ble Indian High Commissioner at London dated 23.05.2003, which was as old as more than two years. However, assessee could not furnish any evidence to demonstrate that new avenue for the activity of the company was explored neither for the year of travel nor for the subsequent year. He, therefore, held that assessee failed to substantiate the nexus of the foreign travel expenses vis-a-vis the business expenditure of

the company. He, therefore, disallowed Rs.13,08,979/- as assessee had already paid FBT of Rs.3,27,244/-. Before Ld. CIT(A), it was pointed out that assessee had filed all evidences, such as, application forms with RBI and the correspondence with Indian High Commission for tour to London of the Director. It was submitted that assessee-company made exports of over Rs.1.00 crore and there was always possibility of increase in exports to other countries considering the nature of product. The Ld. CIT(A) allowed assessee's appeal by observing as under :-

"I have gone through the assessment order and submissions of appellant. I find that there is nothing very unusual about the visit of director of company to visit London in 2005 in continuation of the visit was undertaken in 2003 with reference to start a company in U.K. I find that the visit of the director to U.K. cannot be called a visit for non business purposes merely on the suspicion that a visit after two years of conception of the plan to start a subsidiary company may not be for the same purpose. Therefore, I hold that the visit of the director of appellant company to London is for business purpose in absence of any evidence contrary to the claim of appellant. The details of air ticket submitted by the appellant show that the director departed for London and Edinburgh on 29-05- 2005 and returned to Kolkata on 16-06-2005. The foreign currency withdrawn during this period as per the details submitted by appellant for the boarding and lodging of the director is already estimated to be in the form of perquisite to the director within the provisions of Fringe Benefit Tax and appellant company has already paid Fringe Benefit Tax considering a fringe benefit of Rs.3,27,244/- given by employer appellant company to its director for this tour. There is no need to further estimate any element of perquisite given by appellant to director. Assessing Officer has allowed only the perquisite of Rs.3,27,244/- for deduction and the balance amount of Rs. 13,08,979/- has been wrongly disallowed by him as non business expenditure for the reasons mentioned above. Therefore, I direct the Assessing Officer to allow the expenditure of Rs. 13,08,979/- incurred by appellant company on the tour of its director to U.K. and reduce the total income accordingly."

10. We have considered the submissions of both the parties and have perused the records of the appeal. Admittedly, assessee had shown export turn over of Rs.1.00 crores to UK. Therefore, assessee's claim regarding visit of Director to UK for business purposes can not be doubted. The assessee had produced all the relevant correspondence in this regard which has been taken note of by Ld. CIT(A) and not rebutted by Department. We, therefore, confirm the action of Ld. CIT(A). This ground of Department is dismissed.

11. Ground No.3 reads as under :-

"That in the facts and circumstances of the case and in law, the Ld. CIT(A) has erred in deleting the disallowance of commission of Rs.3,93,3631- u/s. 40A(2)(a) of the Act by holding that the commission paid was not excessive, was allowed in the past, and reflected in the return of income of the recipient, without appreciating the fact that the assessee had failed to produce any evidence for the services rendered for which the commission was paid and the claim of the assessee was inadmissible for this reason."

12. The Assessing Officer noticed that assessee had debited commission of Rs.9,11,432/- in the profit & loss account during the year which included payment of commission of Rs.3,93,363/- to Smt. Kamala Devi Agarwal. The Assessing Officer required the assessee to explain the services rendered by Smt. Kamala Devi Agarwal. The assessee in his submission pointed out that this commission was paid to Smt. Kamala Devi Agarwal @ 1% on turn over of Rs.3,93,36,343/- achieved from outlet at 7, Jagmohan Mallick Lane, Burrabazar, Kolkata-700 007. The amount was paid to her in lieu of services the company

was taking for its benefit and growth. The Assessing Officer, however, did not accept the assessee's explanation observing that no service can be rendered by a lady aged more than 70 years of age that too by a member of the families of status of Shri Prabhu Shankar Agarwal. Ld. CIT(A) allowed the assessee's appeal taking note of the fact that in the assessment of Smt. Kamala Devi Agarwal, the commission had been taxed. Further, the responsibility of growth and profitability of a particular retail outlet of assessee-company had been assigned to Smt. Kamala Devi Agarwal for which she was paid commission of 1% on the turn over. He further pointed out that the Assessing Officer had not made any disallowance on the ground of commission being excessive and unreasonable.

13. We have considered the submissions of both the parties and have perused the records of the appeal. The commission had been paid to mother of Director of assessee-company who has been associated with this business for considerable long time as explained by Ld Counsel. He has pointed out that commission has been paid for the last 25 years and the lady still manages the outlet. Merely her age being 70 years, cannot be a basis for making disallowance. Her presence itself in the outlet was more than sufficient for making the payment of commission to her as she could manage the affairs effectively merely by sitting at the outlet. Though the Assessing Officer has made disallowance by referring to Section 40A(2)(a), but he has not made disallowance on the ground of the same of being excessive and unreasonable. He has made disallowance observing that it was an accommodation of expenses paid to a person satisfied u/s. 40A(2)(a). In our opinion, Assessing Officer has wrongly referred to Section 40A(2)(a) because u/s. 40A(2)(a), disallowance can be made if the expenditure is considered to be excessive and unreasonable having regard to the fair market value of the services rendered by the person. Under such circumstances, we confirm the order of Ld. CIT(A). This ground of the Department is dismissed.

14. In the result, appeal filed by the Department in ITA No.554/Kol/2011 is partly allowed.

15. Now, we shall take up the appeal in ITA No.555/Kol/2011.

16. The first ground of the appeal reads as under :

"That in the facts and circumstances of the case and in law, the Ld. CIT(A) has erred in deleting the addition of Rs.37,56,204/- made on account of low gross profit while holding that assessee had accepted the rejection of books of accounts and without appreciating the materials brought on record and facts evaluated by the AO in the assessment order."

17. Brief facts apropos this issue are identical to the facts as obtained in assessment year 2006-07 with the only difference that Assessing Officer had applied the average G.P. rate of 13.32% as against 12.35% returned by the assessee on the estimated turn over of Rs.35.00 crores as against sales of Rs.34,67,11,839/- shown by the assessee. The addition was deleted by the Ld. CIT(A).

18. After considering the submissions of both the parties, for the detailed reasons given in assessment year 2006-07, we delete the addition made to turn over shown by the assessee and directed the Assessing Officer to adopt G.P. rate of 12.05% as against 12.35% shown by the assessee. This ground of the Department is partly allowed.

19. For the detailed reasons in regard to the ground No.3 for assessment year 2006-07,

this ground is also dismissed.

20. The appeal filed by the Department is partly allowed.

21. In the result, both the appeals filed by the Department are partly allowed.

(Order pronounced in the Court on 28.7.2011.)