IN THE INCOME TAX APPELLATE TRIBUNAL
DIVISION BENCH, CHANDIGARH

BEFORE SHRI BHAVNESH SAINI, JUDICIAL MEMBER
AND MS. RANO JAIN, ACCOUNTANT MEMBER

ITA No.775/Chd/2012
(Assessment Year : 2008-09)

The A.C.I.T., Circle 1(1), Chandigarh.	Vs.	M/s Khandelia Oil & General Mills Pvt. Ltd., Plot No.23, Industrial Area, Phase-II, Chandigarh. PAN: AAACK6655N

And

ITA No.778/Chd/2012
(Assessment Year : 2008-09)

M/s Khandelia Oil & General Mills Pvt. Ltd., Plot No.23, Industrial Area, Phase-II, Chandigarh. PAN: AAACK6655N (Appellant)	Vs.	The Addl.CIT, Range 1, Chandigarh. (Respondent)

Assessee by	:	Shri Anil Khanna
Department by	:	Shri Manjit Singh, DR
Date of hearing	:	09.09.2015
Date of Pronouncement	:	06.11.2015

O R D E R

PER RANO JAIN, A.M. :

Both the cross appeals are directed against the order of learned Commissioner of Income Tax (Appeals), Chandigarh dated 21.5.2012 for assessment year 2008-09.

2. The grounds of appeal raised by the Revenue read as under :

> *"1. The Ld. CIT(A) erred in deleting the addition of Rs. 24,63,106/- made on account of interest paid on unsecured loans u/s 40 A(2)(b).*
>
> *2. The Ld. CIT(A) has erred in deleting the addition of Rs. 53,23,839/- on account of diversion of funds to the sister concerns u/ 36 (i) (iii) or 37 of the Income Tax Act,1961.*
>
> *3. The Ld. CIT(A) has erred in deleting the additions of Rs.3,09,55,904/- made on account of suppression of sales and by not appreciating the facts brought by the A.O. on record.*
>
> *4. The appellant craves to add or amend any ground/grounds of appeal before the appeal is heard or disposed off.*
>
> *5. It is prayed that the order of the Ld. CIT(A) be cancelled and that of the assessing officer may be restored."*

3. The ground No.1 relates to addition of Rs.24,63,106/- made by the Assessing Officer under section 40A(2)(b) of the Income Tax Act, 1961 (in short 'the Act').

4. Briefly, the facts of the case are that out of the total interest on loan, the assessee had paid interest of Rs.1,23,15,529/- on unsecured loans to persons covered under section 40A(2)(b) of the Act. The rate of interest paid was @ 15% per annum. When the Assessing Officer asked the assessee to justify the reasonableness of interest payment @ 15%, it was submitted that the interest paid to the banks on borrowings was @ 10.5%, when the bank loans were against

charge on the property and the opportunity cost on these loans was much more than 15%. It was also submitted that the loans were continuing from earlier years and were instantly available. The Assessing Officer did not find himself in agreement with the submissions of the assessee and restricting the claim of interest to a rate of 12%, made a disallowance of Rs.24,63,106/-.

5. Before the learned CIT (Appeals), the submissions made before the Assessing Officer were reiterated by the assessee. After considering the reply of the assessee the opinion of the learned CIT (Appeals) was that the payment of interest @ 15% was not unreasonable. Based on this, the learned CIT (Appeals) deleted the addition made by the Assessing Officer.

6. The learned D.R. while arguing before us relied upon the order of the Assessing Officer. The learned counsel for the assessee relied upon para 3.2 of the order of the learned CIT (Appeals) and further drew our attention to page 32 of the Paper Book filed by him to emphasize the fact that the rate of interest charged by the Market Committee was 18%. In view of this, it was prayed that the rate of interest charged by the assessee at 15% may be held to be reasonable.

7. We have heard the learned representatives of both the parties, perused the findings of the authorities below and considered the material available on record. Section 40A(2)(b) of the Act is meant to cover cases where interest paid to the

related parties as defined in this section is in excess of the interest paid to unrelated parties. The undisputed fact is that the assessee has paid 15% interest on unsecured loan to persons covered under section 40A(2)(b) of the Act. This is also undisputed that the rate of bank loans are at around 10.5% but this is also a fact that the loans from banks are taken against the charge on the property and there are other opportunity costs involved in raising the loans from the banks, which are not there in the cases of these unsecured loans and the loans from these related persons are instantly available also. Further, since the rate of interest charged by Market Committee itself is 18%, we are in agreement with the findings recorded by the learned CIT (Appeals) that the rate of interest at 15% is quite reasonable. Since the borrowings from private parties are always at higher rate of interest than the banks and these Market Committees. In view of this, order of the learned CIT (Appeals) in this regard is confirmed. The ground of appeal raised by the Revenue is dismissed.

8. The ground of appeal No.2 raised by the Revenue relates to addition of Rs.53,23,839/- made by the Assessing Officer under section 36(1)(iii) of the Act.

9. The brief facts of the case are that there was some outstanding balance in the name of M/s Khandelia Udyog Pvt. Ltd., a sister concern of the assessee. Relying on the judgment of the Hon'ble Punjab & Haryana High Court in the case of CIT Vs. M/s Abhishek Industries Ltd., 286 ITR 1 (P&H), the Assessing Officer disallowed proportionate interest

@ 12% on the debit balance of various branches of M/s Khandelia Udyog Pvt. Ltd. Further, the Assessing Officer noticed that there was a debit balance outstanding in the name of M/s Gauri Shanker & Co., Chandigarh. It was noted that sales had been made to the sister concern during the year but the recovery had not been made in timely manner and debit balance was outstanding throughout the year. In this way, he proportionally disallowed the interest @ 12% on the debit balance of M/s Gauri Shanker & Co. also.

10. Before the learned CIT (Appeals), the submission of the assessee was that these transactions are all in the course of business considering the commercial expediency. The assessee company has made sales and purchases from these concerns. Further the assessee had enough own funds to lend to these concerns and has not used any borrowed funds for this purpose. It was also submitted before the learned CIT (Appeals) that similar issue had come up in appeal before the I.T.A.T., Chandigarh Bench in assessee's own case for assessment year 2006-07 in ITA No.937/Chd/2009, dated 30.4.2010 and the ground was allowed in favour of the assessee. Relying on the said order of the I.T.A.T., Chandigarh Bench, the learned CIT (Appeals) deleted the addition made by the Assessing Officer.

11. The learned D.R. relied upon the order of the Assessing Officer, while the learned counsel for the assessee relied upon the order of the learned CIT (Appeals) and also of

the I.T.A.T., Chandigarh Bench in assessee's own case for assessment year 2006-07 (supra).

12. We have heard the learned representatives of both the parties, perused the findings of the authorities below and considered the material available on record. From the perusal of the order of the I.T.A.T., Chandigarh Bench in assessee's own case for assessment year 2006-07 (supra), we see that the additions in that year were also made on account of proportionate interest on the advances made to the sister concern M/s Gauri Shanker & Co., Chandigarh and transactions with some other parties to whom sales were made. Since in this year also the transaction has been made with M/s Gauri Shanker & Co., Chandigarh and the facts have not been distinguished by any of the lower authorities and even before us, the learned D.R. could not controvert the findings given by the learned CIT (Appeals). With regard to M/s Khandelia Udyog Pvt. Ltd., in the Paper Book filed by the assessee detailed ledger account of the said party has been filed and on perusal of which, we find that the regular sales and purchases are being made from this party through out the year. Therefore, the proposition laid down by the I.T.A.T., Chandigarh Bench M/s Gauri Shanker & Co., Chandigarh can also be applied to M/s Khandelia Udyog Pvt. Ltd. In view of this, we uphold the order of the learned CIT (Appeals) in this regard. The ground of appeal raised by the Revenue is dismissed.

13. The ground of appeal No.3 raised by the Revenue is against the addition of Rs.3,09,55,904/- made by the Assessing Officer on account of suppression of sales.

14. The Assessing Officer noted that during the year the assessee has made substantial portion of the sales i.e. 38.42% to its sister concerns, which were at a very low rate as compared to the sales made to independent parties. In reply, the assessee stated that the sister concerns M/s Gauri Shankar & Co. and also Khandelia Udyog Pvt. Ltd. were returning their income in the highest tax rate slab. Therefore, there was no need for assessee to make sales to them at lower rates. Further, it was argued that these concerns were given trade discounts, therefore, provisions of section 40A(2) of the Act are not applicable to the same. Reliance was placed on the order of the Chandigarh Bench of I.T.A.T. in assessee's case for assessment year 2006-07. The Assessing Officer made a detailed analysis, whereby the sales made to sister concerns and independent parties were compared and examined bill-wise. A few examples as confronted to the assessee are also reproduced in para 5.3 of his order. Rejecting all other contention of the assessee, average percentage was calculated on the basis of samples bills as confronted to the assessee and it was concluded that average suppression in the sales volume is to the tune of 4.34%. Since the assessee had made sale amounting to Rs.71,32,69,682/-, an amount of Rs.3,09,55,904/- was added to the income, being 4.34% of Rs.71,32,69,682/-.

15. Before the learned CIT (Appeals), reply given to the Assessing Officer was reiterated. In addition, it was stated that the contention of the Assessing Officer as regards no difference due to location, it was stated that the loss is incurred in the Chandigarh unit, while the rates compared by the Assessing Officer are that of Sri Ganga Nagar Unit. Further, it was also submitted that booking of freight expenses has no relation with the rate of product as the edible oil being volatile item the rate varies on the basis of demand and supply and rates of the product of the competition in the market at that time at a particular location. Agreeing with the said submission, the learned CIT (Appeals) deleted the addition made by the Assessing Officer.

16. Aggrieved by the same, the Revenue has come in appeal before us.

17. The learned D.R. relied upon the order of the Assessing Officer, while the learned counsel for the assessee relied upon the order of the learned CIT (Appeals).

18. We have heard the learned representatives of both the parties, perused the findings of the authorities below and considered the material available on record. The learned CIT (Appeals) has given a detailed finding with regard to this issue which reads as under :

> *"5.3 I have considered the submission of the Ld. Counsel for the appellant and have gone through the detailed calculation made by the Assessing Officer. The basic point is that an*

assessee cannot be expected, much less be compelled, to make profit in every transaction of sale he makes. However, if the transaction is with a related party and the transaction results in a loss, the onus will be on the assessee to establish that it was a bonafide transaction and was not entered into with the motive of benefitting the related party. In the absence of such evidence being led by the assessee, the revenue will be entitled to disallow/ignore the loss while computing the taxable income. However, if the sales to the related party result in a profit to the assessee, even though the sales are made at a rate, lower than at which the sales are made to other parties, the revenue cannot bring to tax the notional profit which the assessee would or could have earned, had the sales been made at the rates charged from unrelated parties. Having said that, I may add that the appellant has cited many cogent reasons like huge volume of sales to these concerns etc. to justify the sales to the sister concerns at lower rates. It may also be noted here that the Assessing Officer, while calculating the so called suppressed sales, has taken into account the sales made to M/s Gauri Shanker 86 Co., which is an independent and unrelated entity. It may be clarified that while the addition for inflated purchases in respect of purchases made from sister concerns could be made u/s 40A(2)(a), but there is no corresponding provision in respect of sales made to sister concerns. The department cannot compel a person to make profit out of every transaction since the department does not have any authority to ask a person to maximize its profits. If the assessee chooses to give discount to someone, he is free to do it. The only criteria /condition is that the transaction (sale) should not result in loss. This principle was enumerated by the Hon'ble Supreme Court in the case of M/s Calcutta Discount Company Ltd. (91 ITR 8), in which Their Lordships have held that when a trader transfers his goods to another trader at a price which is less than the market price, so long as the transaction is bonafide, the revenue authorities cannot consider the market price ignoring the real price fetched to compute profits from the transaction. It was also held by the

Apex Court in this case that an assessee was at liberty to arrange his affairs so as to minimise his tax burden. In the instant case, the persons to whom sales are made at lower rates are tax payers in the highest marginal tax bracket and so it can not even be viewed as a scheme for tax reduction. In view of this discussion, it is held that the Assessing Officer was not justified in making addition of Rs. 3,09,55,904/- on account of sales made to associated concerns at lower rate and the same is deleted. Ground of appeal No. 4 is allowed."

19. We do not find any infirmity in the order of the learned CIT (Appeals) in this regard. Before us, at Paper Book page 124 a chart explaining in detail the reasons for variation was filed. In fact, the Assessing Officer has tried to bring the provision of domestic Transfer Pricing in this case, where the internal comparables are used. We must mention that the said provisions are not applicable in the year under consideration. We see from the perusal of the detailed reasoning given by the assessee for the difference in rates, that there is no suppression of sales by the assessee. This ground of Revenue is dismissed.

20. The ground Nos.4 and 5 raised by the Revenue are general in nature, hence need no adjudication.

21. The result of the Revenue is dismissed.

ITA No.578/Chd/201 :

22. The grounds of appeal raised by the assessee read as under :

"1. As per the facts and circumstance of the case and as per the provisions of law, the learned COMMISSIONER OF INCOME TAX (APPEALS) has erred upholding the addition of Rs. 1,58,424 made by the assessing officer u/s 14A. The disallowance made be deleted.

2. As per facts and circumstances of the case and provisions of law, the learned COMMISSIONER OF INCOME TAX (APPEALS) has erred in not directing the assessing officer to treat the disallowance of interest u/s 36(1)(iii) as part of Actual Cost and depreciation be allowed on the same.

3. As per facts and circumstances of the case and provisions of law, the learned COMMISSIONER OF INCOME TAX (APPEALS) has erred in sustaining the addition of Rs.61,53,868/- on account of under valuation of closing stock. The addition made be deleted.

4. As per facts and circumstances of the case and provisions of law, the learned COMMISSIONER OF INCOME TAX (APPEALS) has erred in making disallowance of Rs. 18,72,420 out of the commission expenses u/s 37(1) as having not been incurred wholly and exclusively for the purposes of business. The disallowance be deleted.

5. The assessee craves permission to add or amend the above grounds at the time of hearing."

23. The ground No.1 relates to disallowance of Rs.1,58,424/- made by the Assessing Officer invoking the provision of section 14A of the Act.

24. Briefly, the facts are that during the year, the assessee made investments of Rs.66,62,696 in shares and mutual funds. On a query raised by the Assessing Officer,

the assessee submitted that during the year it has earned exempt income amounting to Rs.6,614/- only and it had incurred expenditure in relation to exempt income amounting to Rs.24,288/- only. However, the Assessing Officer rejecting the contention of the assessee, invoking the provisions of Rule 8-D of Income Tax Rules made disallowance of an amount of Rs.1,58,424/-. The learned CIT (Appeals) confirmed the disallowance so made by the Assessing Officer, after considering the detailed submission made by the assessee.

25. The learned counsel for the assessee during the course of hearing took us to the various pages of the Paper Book filed by the assessee. It was shown to us from the perusal of page 15, that the investments during the year were started from 23.11.2007. Further, at Paper Book page 59, a cash flow statement was attached, which showed that cash flow from the operation of the assessee were to the tune of Rs.4,74,33,029/- while the purchase of investments were amounting to Rs.66,61,556/-. This was shown to us to emphasize the fact that no interest bearing funds were utilized for the purposes of investments. In this view, it was prayed that the interest part disallowed by the Assessing Officer under Rule 8D may be deleted. On the expenses part of the disallowance, it was submitted that all along the contention of the assessee before the lower authorities was that it had incurred expenses amounting to Rs.24,288/- for earning exempt income and without recording his satisfaction on how the estimation so made by the assessee was wrong, the

Assessing Officer straightaway made computation as per Rule 8D. Reliance was placed on the judgment of Hon'ble Jurisdictional High Court in the case of CIT Vs. Deepak Mittal. 36CCH 51 (2013) (P&H).

26. The learned D.R. relied upon the order of the lower authorities. His submission was that it is a case of mixed funds being used, therefore, it cannot be said that interest bearing funds were not used for the purposes of investments. Rule 8D is applicable during the relevant assessment year. Therefore, the Assessing Officer was right in invoking the said disallowance and learned CIT (Appeals) has rightly confirmed the same.

27. We have heard the learned representatives of both the parties, perused the findings of the authorities below and considered the material available on record. From the perusal of the ledger account of investments as well as the cash flow statement filed by the assessee, as stated hereinabove, we observe that the amount of investments is miniscule in comparison to the owned funds assessee had. Therefore, it cannot be said that the assessee firm used interest bearing funds for the purposes of making investments. The contention of the learned D.R. as regards availability of mixed funds is also not tenable in view of the latest judgment of the Hon'ble Jurisdictional Punjab & Haryana High Court in the case of Bright Enterprises Pvt. Ltd. Vs. CIT, ITA 224 of 2013 (O&M) dated 27.7.2015, whereby it has been held in very clear terms that in case of availability

of mixed funds presumption to the effect that investments are made out of owned funds has to be taken, as the money has not colour. Moreover in the present case, the learned counsel for the assessee has been able to demonstrate that at the time of making investments, the assessee was having huge amount of owned funds. In view of this, the Assessing Officer cannot make disallowance of interest for the purposes of section 14A of the Act as per Rule 8D. As regards the expenditure part of the disallowance, we agree with the submission of the assessee that nowhere in his order the Assessing Officer has recorded any satisfaction directly or indirectly to the effect why the amount of expenditure incurred for earning exempt income as stated by assessee is not correct. As per the proposition laid down by the Hon'ble Punjab & Haryana High Court in the case of Deepak Mittal (supra), in the absence of such satisfaction, no disallowance of expenses can be made under section 14A of the Act as per Rule 8D. The ground of appeal raised by the assessee is allowed.

28. The learned counsel for the assessee preferred not to press ground No.2 of the appeal. Therefore, the ground No.2 is dismissed as being not pressed.

29. The ground No.3 raised by the assessee is against the addition of Rs.61,53,868/- made by the Assessing Officer on account of undervaluation of stock

30. The brief facts of the case are that the Assessing Officer during the assessment proceedings noticed that the assessee was valuing raw material and packing material at cost and the finished goods at estimated cost or net realizable value, whichever was lower. He also found that the assessee was not following any systematic method for valuation of closing stock, which should have been as per the FIFO method. He also noticed that a large number of expenses like, packaging, freight, faxes, etc. have not been loaded to the closing stock. After examining the sample of purchase and sale bills, the Assessing Officer concluded that there is an average undervaluation of stock @ 11.76% and this way, he made an addition of Rs.61,53,868/-.

31. Before the learned CIT (Appeals), the assessee made detailed submissions and tried to find out the fallacy in the method adopted by the Assessing Officer to calculate the undervaluation of stock. The contention of the assessee was that the Assessing Officer had on the basis of arbitrary and illogical assumptions had calculated valuation of stock while the assessee has been adopting the same method consistently over the past many years, which has been all along accepted by the Department. Further, explanation of each and every component of raw material and finished goods was submitted before the learned CIT (Appeals). Rejecting all the contention of the assessee, the learned CIT (Appeals) held that the assessee had not followed any method for the purposes of valuation of closing stock which should have been valued as

per FIFO method. Further, he observed that the assessee has not been able to explain as to how the Assessing Officer was not right in observing that the assessee had valued the closing stock of mustard seed @ Rs.2472 per qtl. as against Rs.2638 per qtl. as per the purchase bills in the month of March, 2008. Further referring to the detailed working done by the Assessing Officer, the learned CIT (Appeals) confirmed the addition.

32. The learned counsel for the assessee reiterated the submissions made before the lower authorities and further to explain the discrepancy as in the valuation of stock by the assessee and that of the Assessing Officer, he filed a detailed chart of each and every item of raw material and finished goods purchased by it. It was stated before us hat the assessee has been adopting the same method of valuing the stock consistently in the last many years and there is no law, which provides to value the stock mandatorily as per FIFO method. Further, the observation of the learned CIT (Appeals) that the assessee had not been able to controvert the variation in mustard seed @ Rs.2472 per qtl. taken by the Assessing Officer as against Rs.2638/- per qtl. taken by the assessee. It was submitted that the Assessing Officer himself mentioned that the stock should be valued as per FIFO method, while he has taken the average of the rates of last three bills and concluded the undervaluation. Further, certain pages of the Paper Book were referred to show that the expenses have been properly loaded in the valuation of closing

stock. In this way, it was prayed that there being no error in the method followed by the assessee to value the closing stock, the addition made by the Assessing Officer be deleted.

33. The learned D.R. relied upon the orders of the Assessing Officer as well as of the learned CIT (Appeals).

34. We have heard the learned representatives of both the parties, perused the findings of the authorities below and considered the material available on record. First of all, the premises upon which the issue was initiated by the Assessing Officer, that the assessee should follow FIFO system of accounting for valuing closing stock itself is not correct. Nowhere in the Income Tax any such method is prescribed. Only requirement is to adopt a generally accepted accounting policy on a consistent basis. The assessee has been following the practice of stock valuation consistently, which has been accepted by the department in earlier years also. We also observe a contradiction in the stand of the Assessing Officer. He himself mandates to follow the FIFO method. However, he himself takes an average of the last few bills for valuing the stock of raw material. Further, he takes the bill of oil dated 6.3.2008 and not of 31.3.2008. We have perused the details filed by the assessee, whereby it is seen that all relevant expenses have been considered for valuing stock. Therefore, the observation of the Assessing Officer that expenses have not been loaded is also not correct. Further, the difference worked out in respect of oil, has been applied to all categories of stock i.e. oil cakes, de-oiled cakes, stock in process etc.

This all shows the lack-luster approach, which has been adopted by the Assessing Officer for working out the difference in valuation of stock. On the other hand, the assessee has filed before the lower authorities all details pertaining to basis of valuation of stock of various items. These basis have been explained to us during the course of hearing in great detail. We do not find any irregularity in the same. In view of this, the addition made by the Assessing Officer is hereby deleted.

35. The ground No.4 raised by the assessee is against the disallowance of Rs.18,72,420/- made by the Assessing Officer on account of commission expenses.

36. The brief facts of the case are that during the relevant assessment year, the assessee paid commission to the following persons :

(i)	Shri Anil Rastogi, Delhi	Rs.7,79,011/-
(ii)	Shri Yogesh HUF, Delhi	Rs.3,74,977/-
(iii)	Shri Yogeh Trading Co., Parwanoo.	Rs.7,18,432/-
		Rs.18,72,420/-

37. The Assessing Officer observed that the persons mentioned at Sr.No.(ii) and (iii) are also covered under section 40A(2)(b) of the Act. The assessee could not find any details of services rendered by these persons. Further, it was also observed by the Assessing Officer that since the assessee has not made any substantial sale in Delhi, the payment of commission to Shri Anil Rastogi was not justified. In this

way, he disallowed the total amount of Rs.18,72,420/- being commission expenses claimed by the assessee.

38. Before the learned CIT (Appeals), it was clarified that the payment of commission to Shri Anil Rastogi was on account of sale made in the territory of West Bengal, the address of Shri Anil Rastogi may be of Delhi. The confirmations from the commission agents were also filed before the learned CIT (Appeals). However, the learned CIT (Appeals) did not filed himself in agreement with the assessee. Stating that the confirmations were additional evidences and since the assessee has not given any plausible reason for not filing the same during the course of assessment proceedings, he confirmed the disallowance.

39. The learned counsel for the assessee prayed before us that the learned CIT (Appeals) may be directed to admit the additional evidences. While learned D.R. opposed the said stance of the learned counsel for the assessee.

40. We have heard the learned representatives of both the parties, perused the findings of the authorities below and considered the material available on record. We observe from the order of the lower authorities that the disallowance on account of commission paid to Shri Anil Rastogi on the basis that his address is in Delhi, while the assessee has not made any sale in Delhi is not correct. It may be that the address is of Delhi, but Shri Anil Rastogi must be operating in West Bengal also. This issue has not been dealt with by the lower

authorities in right perspective. Further, the confirmations filed by the assessee before the learned CIT (Appeals) were not admitted. In the interest of justice, we restore the issue back to the file of the learned CIT (Appeals) to consider afresh. The assessee is at liberty to produce evidence and material to defend its case. It may be given proper opportunity of being heard.

41. The appeal of the assessee is partly allowed.

42. In the result, the appeal of the Revenue in ITA No.775/|Chd/2012 is dismissed and the appeal of the assessee in ITA No.778/Chd/2012 is partly allowed,

Order pronounced in the open court on this ..... day of November, 2015.

Sd/-	Sd/-
(BHAVNESH SAINI)	**(RANO JAIN)**
JUDICIAL MEMBER	**ACCOUNTANT MEMBER**

Dated : 6th November, 2015

Rati

Copy to: The Appellant/The Respondent/The CIT(A)/The CIT/The DR.

Assistant Registrar,
ITAT, Chandigarh