

IN THE INCOME TAX APPELLATE TRIBUNAL
HYDERABAD BENCHES "A" : HYDERABAD

BEFORE SHRI SAKTIJIT DEY, JUDICIAL MEMBER
AND
SHRI INTURI RAMA RAO, ACCOUNTANT MEMBER

ITA.No.1480/Hyd/2014
Assessment Year 2007-2008

KLR Industries Ltd., Hyderabad PAN AABCK7920K (Appellant)	vs.	DCIT, Central Circle 2(1), Hyderabad. (Respondent)
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For Assessee :	Mr. A.V. Raghuram & Mr. T. Chaitanya Kumar
For Revenue :	Mr. D. Srinivasa

Date of Hearing :	04.06.2015
Date of Pronouncement :	15.07.2015

ORDER

PER SAKTIJIT DEY, J.M.

This appeal by the assessee is directed against the order dated 08.08.2014 of Id. CIT(A)-IV, Hyderabad for AY 2007-08.

2. As per the revised grounds of appeal, assessee has raised the following grounds:

- 1. "On the facts and in the circumstances of the case, the order of the learned V Commissioner of Income-Tax (Appeals) is erroneous, illegal and unsustainable in law.*
- 2. The learned Commissioner of Income-Tax (Appeals) erred in sustaining the addition*

made the Assessing Officer of Rs 9,78,50,000/- as unexplained credits under section 68 of the Income Tax Act. The learned Commissioner (Appeals) failed to appreciate that the persons who have invested the amounts in the share capital of the Appellant Company are men of means and are income tax assesseees and therefore the addition could not have been made in the hands of the Appellant.

- 3. The Learned Commissioner (Appeals) erred in sustaining the addition of Rs 6,51,93,703/- in respect of trade credits. The Commissioner (Appeals) failed to appreciate that the parameters applied for making addition under section 68 of the Income Tax Act, cannot be applied with equal force to the trade credits.*
- 4. The Learned Commissioner Of Income Tax (Appeals) erred in sustaining the disallowance of the interest expenditure of Rs 55,69,108/- on the alleged ground that they are not advanced in the course of business.*
- 5. The learned Commissioner Of Income tax(Appeals) erred in setting aside the addition an amount of Rs 8,92,937/- being the payment made towards hire purchase installment on vehicles. Having regard to the Board Circular which was referred to in the appellate order, the learned CIT(A) ought to have deleted the disallowance made by the Assessing Officer”.*

2.1. In addition, assessee has also sought permission to raise the following additional grounds:

ADDITIONAL GROUNDS

6. *“Without prejudice to ground no.5 raised above, the learned Commissioner (Appeals) failed to appreciate that the above payment towards hire purchase installments on vehicles could not have been disallowed in view of the fact that no amount remained payable as at the end of the year. It any rate the learned Commissioner (Appeals) further failed to appreciate that pursuant to insertion of second proviso to section 40a(ia) of the Income Tax Act, which is held to be retrospective in operation, no disallowance can be made unless an order is passed under section 201(1) of the Income Tax Act holding the Appellant to be 'assessee in default'.*
7. *The learned Commissioner (Appeals)/ Assessing Officer erred in disallowing an amount of Rs 53,58,187/- as bad and doubtful debts without appreciating the fact that under the provisions of section 36(1)(vii) of the Income Tax Act it is not essential for the Appellant to prove the fact of debt becoming bad to the hilt and it is sufficient if the Appellant has offered the income and has written it off as bad and doubtful in its books of account.*
8. *The The learned Commissioner (Appeals) / Assessing Officer erred in disallowing interest on car finance paid to various banks amount to Rs.3,78,909, interest on loan paid to Ramireddy of Rs.12,00,000 and to Prem Raj at Rs.75,000 under the provisions of section 40a(ia) of the Income Tax Act.*
9. *On the facts and in the circumstances of the case the learned Commissioner (Appeals) / Assessing Officer erred in disallowing the fee*

of Rs.3,01,452 paid for increase of share capital.

10. On the facts and in the circumstances of the case the learned Commissioner (Appeals) / Assessing Officer erred in disallowing Rs.2,07,209 being the employees contributions to ESI and Provident Fund beyond due dates prescribed under respective statutes, but paid before filing the return of income under the Income Tax Act.”

2.2. Assessee has also filed a petition under Rule-11 of the ITAT Rules, 1963 explaining the reasons why additional grounds could not be raised before Id. CIT(A).

3. After hearing the submissions of the parties, we are inclined to admit the additional grounds of assessee considering the fact that the issues raised therein arise out of the assessment order and can be decided on the basis of the facts and materials available on record.

4. As far as the main grounds are concerned, Ground No. 1 being general in nature do not require any specific adjudication.

5. In Ground No. 2, assessee has challenged the addition made of an amount of Rs. 9,78,58,000 as unexplained cash credit u/s 68 of the Act.

6. Briefly, the facts relating to this issue are, assessee a company is in the business of

manufacturing of earth boring and drilling equipments. For the impugned assessment year, assessee filed its return of income on 15.11.2007 declaring total income of Rs.3,05,94,470. During the assessment proceeding, AO noticed that assessee, in the PY relevant to AY under dispute, has introduced an amount of Rs.9,88,50,000 as share application money in its books of account. From the details furnished by assessee, AO found that the amount has been introduced in the names of 19 persons as under:

Sl.No.	Name of share applicant	Amount
1.	Rajeswari Enterprises	44,25,482
2.	A Krishna Reddy	90,00,000
3.	Prem Raj	50,00,000
4.	Rupireddy Shantha	34,00,000
5.	Vasanthi Kochar	5,00,000
6.	Vani Mudha	30,00,000
7.	R Rashmi Reddy	5,00,000
8.	Vijay Kochar	5,00,000
9.	Pedda Gollabab	34,30,000
10.	Lachi Reddy	2,02,05,371
11.	Ravi Reddy Laboratory	20,00,000
12.	Rajadhani Sanjai	41,00,000
13.	Madan Mohan Rao	42,65,909
14.	Chakravardhan	40,00,000
15.	A.V. Reddy	2,00,00,000
16.	K Laxma Reddy	14,12,117
17.	B Arjun Reddy	1,60,00,000
18.	Krishi Enterprises	19,20,000
19.	K. Vijaya Laxmi	3,50,121

7. To a query raised by AO, it was explained by assessee that during relevant financial year, two

of its Directors, namely Shri K. Laxma Reddy and Smt. Vijay Laxma Reddy have brought in share capital to the tune of Rs. 9,88,50,000 consisting of their individual contribution of Rs. 19,44,371 and Rs. 3,57,121 respectively and the amounts borrowed from different individuals amounting to Rs. 9,65,48,508 to meet the fund requirement of the company for its business operation. It was further submitted, company had received the said amount by cheques/drafts from time to time and deposited into the company's account. However, under personal agreement with the persons concerned, both the Directors have undertaken to repay the said amount individually by themselves and advised the company to treat the said monies received by company as their share application money. On examining the submissions of assessee, AO observed that assessee has not produced copies of the personal agreements entered by Directors with various individuals nor it has produced communication with various creditors. Therefore, AO called upon assessee to prove identity of share applicants and their creditworthiness as well as genuineness of the transaction. In response to the query made, as observed by A.O. in the assessment order, assessee submitted confirmation letters in respect of the following 7 persons covering an amount of Rs.2,95,91,391.

Sl.No.	Name of share applicant	Amount
1.	Rajeswari Enterprises	44,25,482
2.	A Krishna Reddy	90,00,000
3.	Prem Raj	50,00,000
4.	Rupireddy Shantha	34,00,000
5.	Vasanthi Kochar	5,00,000
6.	Vani Mudha	30,00,000
7.	Madan Mohan Rao	42,65,909
	Total	2,95,91,391

8. Assessing Officer after verifying the confirmation letters, observed that though the creditors/share applicants have confirmed of having advanced amounts to one of the Directors Shri K. Laxma Reddy for investing in the company, but, none of them have explained the source of the amounts advanced. He also observed, assessee could not file any evidence to prove the creditworthiness of the share applicants. Thus, AO observed that even though all the creditors/share applicants are assessed to tax, but, since the amounts advanced are huge without verifying their source of income, amounts advanced by them cannot be treated as genuine. Further, AO observed that assessee did not furnish confirmation letters in respect of 12 creditors/share applicants for credit amounting to Rs.7,44,17,609. Stating that onus is on assessee to substantiate the amounts introduced in its books of account, AO held that assessee having failed to discharge the onus of proving genuineness of credits, share application money

amounting to Rs.7,44,17,609 has to be treated as assessee's income for the AY under consideration. Assessee challenged the addition made before ld. CIT(A).

9. In course of hearing of appeal before ld. CIT(A), assessee submitted confirmation letters in respect of 12 share applicants/creditors for the amount of Rs.7,44,17,609, which could not be produced at the time of assessment proceeding. On the basis of the confirmation letters submitted by assessee, Ld. CIT(A) called for remand report from A.O. After perusing the remand report of A.O, ld. CIT(A) found that in case of Shri R. Rashmi Reddy, advance of Rs. 5 lakh was made in AY 2005-06. Therefore, since the credit does not pertain to the year under consideration, ld. CIT(A) deleted the addition of Rs. 5 lakh. Similarly, in case of Shri Vijay Kochar, it was found on examination that Rs. 5 lakh credit appearing in his name has been brought forward from earlier year. Accordingly, ld.CIT(A) deleted the amount of Rs.5 lakh appearing in the name of Shri Vijay Kochar. As far as the rest of the creditors are concerned, ld. CIT(A) observed that A.O. in his report has pointed out that information submitted by assessee do not substantiate the genuineness of the transaction and creditworthiness of the creditors. He also referred to the observation of A.O. to the effect that assessee

has not furnished share applications made by investors nor produced any evidence to show that shares were allotted to them. When these facts were confronted to assessee, he submitted that when the confirmations have been filed from the creditors/ share applicants disclosing their identity, income-tax particulars and also admitting the fact that they have advanced money and more over when the entire transactions are through banking channels by way of account payee cheque/drafts and when affidavits have been filed to prove the genuineness of the transaction and creditworthiness of the creditors, amounts appearing in the books of account as share application money cannot be treated as unexplained credit. In support of such contention, assessee relied upon certain judicial precedents.

10. Ld.CIT(A) after considering the submissions in the light of the facts and materials on record as well as report submitted by AO, though, acknowledged the fact that identity of the creditors have been established by furnishing PAN, addresses and assessment details, but, as far as the creditworthiness of the creditors is concerned, no evidence has been furnished by assessee. Ld. CIT(A) was of the view that when assessee had stated that Directors undertook to pay the said amount individually by themselves and advised the company

to treat the money as share application money, then, how could it be treated as share application money. He observed that the statement given by director indicate that these are loans taken by Directors in their individual capacity, but, they have advised the company to treat them as share application money. Ld. CIT(A) observed that except the claim made by assessee as regards share application money no material has been filed to prove that these amounts have been invested by share applicants for buying shares of the company. He noted that the confirmation letters from the parties confirmed that the amounts are paid to Shri K. Laxma Reddy for the purpose of investment in the company and does not indicate that the amounts paid are share application money for the purpose of buying the shares of the company. Ld. CIT(A) observed that assessee even did not produce before A.O. personal agreements claimed to have been entered by the Directors with the parties in this regard. Thus, ld. CIT(A) by observing that onus is on assessee to prove that credits appearing in the books of account are share application money, which assessee has failed to discharge, confirmed the addition of Rs.7,44,34,609. As far as the amount of Rs.2,95,91,391 representing the investment made by seven persons in whose case confirmation letters were filed before AO, but,

additions were not made, Ld. CIT(A) observed that in the remand report, AO has stated that genuineness of the transactions relating to the aforesaid amount is not established, hence, the amount of Rs. 2,95,91,391, though was not added at the time of assessment proceeding, also needs to be treated as unexplained credit and added to the income of assessee. Ld. CIT(A) following the observations in case of other creditors, also treated the amount of Rs. 2,95,91,391 as unexplained u/s 68 of the Act. Being aggrieved of the order of ld. CIT(A), assessee is before us.

11. Ld. AR strongly challenging the finding of the A.O. and ld. CIT(A) submitted before us, actually the Directors of the company have contacted number of persons and received advances from them for investment in the company which was shown as investment towards share application money. It was submitted, before AO assessee has produced confirmation letters in respect of 7 persons/creditors/share applicants with their names, addresses, PAN and assessment particulars, etc. wherein they have categorically stated of having advanced the amounts to assessee through director. Before Ld.CIT(A), assessee has submitted confirmations with all the above particulars in respect of rest of the creditors. Ld. AR submitted, when assessee has disclosed identity of the

creditors with assessment particulars and all other necessary details with their bank account copies and when the creditors have confirmed of having made investment in the company, it cannot be said that assessee has failed to discharge its onus of providing cash credits. Ld. AR submitted, as far as the ingredients of section 68 are concerned, assessee has fulfilled the first ingredient of establishing identity of creditors which also the department has accepted. As far as the second ingredient, genuineness of the transactions is concerned, there cannot be any doubt with regard to the same as each of the transaction is through regular banking channel by way of account payee cheque/draft and credit entries are appearing in the respective bank accounts. Therefore, the only other ingredient remains to be fulfilled is creditworthiness of the creditor. Ld. AR submitted, when all the creditors have confirmed of having advanced the amount and it is reflected in their respective accounts and more over when all the creditors are income-tax assesseees, no doubt can be raised with regard to their creditworthiness. Moreover, assessee having discharged the initial onus cast upon it, it cannot be expected to prove the source of source. Ld. AR submitted, if at all there is any doubt with regard to the source from which creditors have advanced the money, then, action has to be taken

against them instead of assessee. As far as the allegation of ld. CIT(A) that though assessee has claimed the credits to be towards share application money whereas the confirmations show they as investments, ld. AR submitted, whether it is share application money or investment, addition cannot be made at the hands of assessee u/s 68 if the ingredients of the said provision are not attracted. He, therefore, submitted, no addition can be made u/s 68 of the Act.

12. Ld. CIT/DR on the other hand, defending the order passed by him submitted, the assessee though, introduced the amount in question as share application money but he failed to prove such credit through proper documentary evidence at any stage of the proceeding. Ld. D.R. submitted, though, assessee produced confirmation letters from the creditors and also furnished their income tax particulars, but, none of the creditors admitted of having advanced the amount as share application money. He submitted that onus is on assessee to prove cash credit appearing his books not only by establishing the identity and creditworthiness of creditors but also the genuineness of the transaction. He submitted, as the assessee has failed to prove the creditworthiness of the creditors, conditions of section 68 are satisfied and amount credited was rightly treated as unexplained cash

credit. The Ld. D.R. relying upon a decision of Hon'ble Supreme Court in the case of Rajendran Chingaravelu vs. Addl. CIT & Others (2010) 320 ITR 1 (S.C.) submitted that income tax authorities are well within their powers to not only satisfy themselves that money is from legitimate source, but also satisfy themselves that money is going to be utilized for legitimate purpose. Thus, he finally concluded that the assessee having failed to explain the credit, addition is justified.

13. We have considered the rival submissions and perused the orders of the revenue authorities as well as other materials placed on record. We have also applied our mind to the decisions relied upon by the learned A.R. As could be seen, the A.O. in course of assessment proceedings finding that the assessee during the relevant previous year has introduced an amount of Rs.9,88,50,000 as share application money in the name of 19 persons enquired into the source of such credit and ultimately concluded that assessee's claim that they represent share application money received from certain persons cannot be accepted and accordingly treated them as unexplained cash credit under section 68 of the Act. Learned CIT(A) also confirmed such addition. As can be seen from the materials available on record, before the A.O. assessee submitted confirmation letters in case of seven

persons covering an amount of Rs.2,95,91,391. In course of hearing of appeal before the first appellate authority, the assessee submitted confirmation letters containing not only the name, address of the party, but also the income tax particulars including PAN. In addition to the confirmation letters, the assessee also submitted affidavits of the concerned persons confirming advancing of money along with other necessary details like the mode of advancement of money, account copies etc., before the first appellate authority. As it appears the A.O. as well as Ld. CIT(A) only emphasizing on the fact that in the confirmation letters, the concerned persons have stated of having advanced the amounts towards investment whereas, the assessee in its books has shown the amount as share application money, which according to the A.O. and learned CIT(A) the assessee has failed to substantiate through documentary evidence, the credits have been treated as unexplained cash credits under section 68 of the Act. It is evident from record, in course of proceeding before departmental authorities, it was explained by the assessee that the advances were actually obtained by the Director's from their known persons and on their advice it was shown as share application money in the books of the company since capital was required for the company to diversify its

activities to real estate business. It is a fact on record that all the creditors have not only confirmed of having advanced the amount in question, but the entire transaction is through proper banking channel by way of cheque or DD.

13.1. It is a well known principle of law that for establishing a credit appearing in the books of accounts, the initial onus is on the assessee to prove such credit by establishing the identity of the creditor, the genuineness of the transaction and the creditworthiness of the creditor. In the facts of the present case, it is a matter of record that the assessee has produced confirmation letters in respect of all the creditors wherein not only the identity of the creditors with their address have been furnished but income tax particulars including PAN has also been given. Therefore, the identity of the creditors remains established. In fact learned CIT(A) has also accepted this position. The second ingredient which requires fulfillment is the genuineness of the transaction. As is evident, the entire transaction has been through proper banking channel. Therefore, as far as the assessee is concerned, the genuineness of the transaction has been established as not only the transaction is through banking channel but the source of such credit has also been proved by the assessee. Now coming to the third ingredient, the creditworthiness

of the creditors, it is to be noted that all the creditors have not only confirmed of having advanced the money to the assessee but have also stated that it is out of their own sources. It is also not disputed that all the creditors are income tax assesseees' in the role of the department.

13.2. As it appears from the orders of the A.O. as well as CIT(A) as well as the remand report submitted by the A.O., the primary reason for not accepting assessee's explanation is creditworthiness has not been proved. If at all the A.O. or Ld. CIT(A) had any doubt with regard to creditworthiness of the creditors, it should have triggered an enquiry by the A.O. to find out the real facts. When the identity of the creditors along with their income tax particulars including PAN and assessment details were available with the A.O. it would not have been difficult on the part of the A.O. to verify their bank accounts and other details to ascertain whether the advances were from explained sources. Even the A.O. could have taken up the issue with the concerned A.Os with whom the creditors are assessed. When all the creditors are assesseees' of the Income Tax Department and the entire transaction is through proper banking channel, it is not understood how the A.O. and Ld. CIT(A) could doubt the creditworthiness of the concerned creditors without bringing any positive evidence or

material on record through a process of enquiry to indicate that the creditors did not have the creditworthiness to advance the amount. It further needs to be mentioned, when the entire transaction is through proper banking channel, it is for the department to bring positive evidence on record to establish that it is the assessee's money which has been routed back to him through the creditors.

13.3. In our view, though, the assessee has discharged the primary onus cast upon it by establishing the identity of the creditors, the genuineness of the transaction and the source from which the credit has come, but the department has miserably failed to prove the fact that the creditors do not have the creditworthiness or the transaction is not genuine. Only because the credits have been shown as share application money in the books of accounts of the assessee, it will not automatically lead to the conclusion that the amount received is unexplained credit as the assessee has failed to establish its claim that the money advanced is towards share application money. Regardless, whether the advances were towards share application, as claimed by the assessee, or investment as stated by the creditors in the confirmation letters and affidavits, fact remains that the assessee has proved the source from which such credit has come to him. Moreover, it is not in

dispute that in addition to the confirmation letters and other evidences filed, the assessee in course of proceeding before Ld. CIT(A) has also produced affidavits from the concerned parties wherein they have accepted that the amounts were advanced by them towards investment in the company. Ld. CIT(A) has refused to take cognizance of the affidavit by stating that they are in the nature of additional evidence. In our view, when certain statements have been made in the affidavit which are only supporting the confirmation letters already filed, they cannot be ignored by treating them as additional evidence. The averments made in an affidavit prima facie has to be considered to be correct unless evidence is brought on record to falsify the claim made in the affidavit. At this juncture, it needs to be mention that in course of hearing before us, Ld. CIT/D.R. submitted that though the assessee was asked by the department to produce creditors for examination, but assessee failed to produce them. Since, learned Counsel appearing for the assessee strongly denied and disputed the aforesaid claim of the Ld.CIT/D.R., the Bench made a specific query to the learned D.R. to produce evidence before the Bench by way of order sheet entry or communication made to the assessee to indicate that assessee was asked to produce creditors for examination. Though, Ld.D.R. stated

before us that such evidence would be brought to record by way of written submission but till date neither any written submission or evidence have been filed before us by the Ld. CIT/D.R. Thus, from the aforesaid facts, a conclusion can be drawn that the assessee was never asked to produce the creditors. If the department had any doubt with regard to the genuineness of the transaction or creditworthiness of the creditors, they should have made proper enquiry and brought positive material on record to establish such fact. More so, when not only the identity of the creditors are available with the department, but their income tax particulars are also submitted by the assessee. The department could have also made enquiry with regard to the source of the money advanced as it was through proper banking channel and could have ascertained whether there is a nexus between the unaccounted income of the assessee and the money advanced. Without any such enquiry, the department cannot be permitted to treat the credit as unexplained income of the assessee on mere presumption and surmises or solely relying upon the entries made in the books of account showing the credit as share application money. In the aforesaid facts and circumstances, the assessee having proved the credits by establishing the identity of the creditors, genuineness of the transaction and

creditworthiness of the creditors, through proper documentary evidence, he is not required to prove any further. As far as decision relied upon by Ld. D.R. is concerned, on careful analysis of the same, we fail to understand how it will apply to the facts of the present case. Therefore, on overall consideration of facts and materials on record, we are of the view that no addition under section 68 of the Act can be made in the present case. Accordingly, we delete the addition made by the departmental authorities and allow the ground of the assessee.

14. In ground No.3 of the revised ground, the assessee has challenged the addition made of Rs.6,51,93,703 as unexplained credit under section 68 of the Act.

15. Briefly the facts are during the assessment proceedings, the A.O. while verifying the accounts of the assessee noticed that assessee has shown an amount of Rs.12,41,93,703 as trade credits in the name of 11 persons. When called upon to explain the source of such credits, it was submitted by the assessee that during the year assessee became interested in real estate business, for which purpose, it accepted advances from certain parties which were shown as credit deposits. The A.O. however was of the view that the amount

introduced are in the nature of cash credit, hence, called upon the assessee to prove the identity, creditworthiness of the creditor and genuineness of the transaction. In response to query raised by the A.O. assessee submitted confirmation letters from two parties for an amount of Rs.5,90,00,000. However, as far as other credits are concerned, as observed by the A.O., the assessee could not even submit confirmation letters. Keeping this fact in view, the A.O. while accepting the credits of Rs.5,90,00,000, treated the balance amount of Rs.6,51,93,703 as unexplained cash credit under section 68 of the Act and added it to the income of the assessee. Being aggrieved of such addition, assessee preferred appeal before the first appellate authority.

16. In course of hearing of appeal before the first appellate authority, out of the 9 persons in whose cases assessee could not produce confirmation letters before the A.O., assessee produced confirmation letters in respect of six persons for credit amount of Rs.6,23,24,518. On the basis of the submissions made by the assessee and evidences produced, Ld. CIT(A) called for a remand report. In the remand report, the A.O. stated that though the assessee has established the identity of the creditors, but, he has failed to establish the creditworthiness of the creditors and genuineness of

the transaction. Learned CIT(A) after considering the report of the A.O. confirmed the addition by observing that assessee has failed to prove the creditworthiness of the creditors and genuineness of the transaction.

17. We have considered the submissions of the parties and perused the orders of the authorities and other materials available on record. The Learned Counsel for both the sides adopted the arguments advanced in case of cash credit. In addition, learned A.R. submitted that the ingredients of section 68 cannot be applied to trade credits as it is in course of business transaction. The learned A.R. submitted that the amounts were received as advance towards real estate business/development activities to be undertaken by the assessee. In this context, he not only relied upon the confirmation letters but also copy of development agreement entered with some of the parties. On perusal of assessment order, it is very much clear that the A.O. has disallowed the amount of Rs.6,23,24,518 only for the reason that the assessee has failed to submit confirmation letters from the concerned creditors, whereas, he accepted the credits in respect of which, the assessee could submit confirmation letters. On going through the confirmation letters, it is very much evident that not only the creditors have confirmed of giving

advance to the assessee, but it is also evident that all of them are income tax assessee's as well as the transaction is through proper banking channel. On a perusal of a sample copy of the registered development agreement between the assessee and M/s. Suchir India Developers P. Ltd., a copy of which is placed on record, the claim of the assessee that these are trade credits cannot be disbelieved. Even assuming that the credits are not trade advance, fact remains assessee has produced documentary evidence to establish the identity of the creditors by furnishing their postal address as well as PAN with income tax particulars. It is also not disputed that the advances were received through proper banking channel, hence, genuineness of the transaction also cannot be doubted. Therefore, if the A.O. had any doubt with regard to the creditworthiness, he should have made proper enquiry with the concerned person to find out whether they had the capability to advance the amount to the assessee. The material on record demonstrate that A.O. without making any enquiry has made the addition merely on presumption and surmises. In case of trade credits also assessee has established the identity of the creditors by furnishing confirmation letters containing their name, address, income tax particulars etc. The entire transaction is through proper banking

channel, thereby, proving its genuineness. Lastly, all creditors are income tax assesseees which prove the source of credits. Therefore, following our detailed reasoning in paragraph Nos.13 to 13.3 in case of share application money, which also equally applies to the trade creditors, we delete the addition of Rs.6,23,24,518. However, in respect of three creditors viz., Palomi Estates, Zisanuddin and others for a total amount of Rs.28,69,185, it is a fact on record that assessee has neither furnished any confirmation letters nor any other evidence to establish the identity of the creditors, their creditworthiness and genuineness of the transaction. Therefore, in absence of any evidence submitted by assessee to prove the credits for the aforesaid amount, addition to the extent of Rs.28,69,185 is sustained. This ground is partly allowed.

18. In Ground No.4, assessee has challenged the disallowance of an amount of Rs.55,69,108 out of the interest expenditure claimed during the year.

19. Briefly the facts are, during the assessment proceeding, the A.O. while verifying the balance sheet of the company along with the books of account noticed that during the year assessee has made the following investments out of the borrowed funds :

Sl.No.	Name	Amount
2.	KLR Mining Equipments Ltd.,	1,32,86,987
3.	SBI One India Fund	1,00,000
4.	Palaka Estate	8,22,250
5.	Dubai Investment	2,21,00,000
	Total	3,63,09,237

19.1. When the A.O. called upon the assessee to explain why proportionate amount out of the interest expenditure shall not be disallowed, as investments made with sister concerns/related parties were not for business purpose, it was submitted by the assessee that the investments in Dubai were made to acquire an industrial facility in a free trade zone with a view to facilitate assembly of equipment exported by assessee company and market the products as made in UAE. The A.O. observed that the assessee did not adduce any evidence to show that the investment made is for the purpose of assessee's business. Further he opined that even if it is accepted that assessee has utilized the investment for assembling equipment in an industrial unit in Dubai but the same is going to be a separate entity taxable under the tax laws of UAE. Therefore, for acquiring industrial facility in Dubai, which is going to be a separate entity, cannot be treated as funds utilized for the purpose of assessee's business.

19.2. As far as investment in KLR Mining Equipment is concerned, it was submitted by the assessee that the amount was advanced to clear/pay off the liability of the concerned party to bank and to pay for the personnel employed by it. It was explained by the assessee that investment was necessary to meet such liability as the assessee was operating from the same premises and in the event, the property is attached by the bank for recovery of their dues, then, the business of the assessee would have suffered. It was submitted, since the investment was made for safeguarding the property and assets of the company, the amount advanced is for the purpose of business. The A.O. however, did not find merit in the submissions of the assessee. He observed that when interest bearing funds of assessee were utilized to meet liabilities of another company, it cannot be for the purpose of assessee's business. As far as investments in Palaka Estate and SBI-ONE India Fund is concerned, the A.O. observed that the assessee did not offer any explanation regarding the nature of investment. The A.O. therefore, referring to the provisions of section 36(iii) of the Act held that since the assessee has utilized borrowed fund to the extent of Rs.3,63,09,237 not for business purposes, proportionate interest calculated at the rate of 12% on such investment made has to be disallowed out

of the total interest expenditure claimed by the assessee. Accordingly, the A.O. worked out the disallowance at Rs.43,57,108. The A.O. also found that during the year assessee has made personal advances to Sanjay Kumar Jain and Rashmi Reddy amounting to Rs.56 lakhs and Rs.45 lakhs respectively. The A.O. observed that personal advances cannot be treated as funds utilized for business and accordingly worked out proportionate disallowance from interest expenditure at Rs.12,12,000. Therefore, the total disallowance made by the A.O. was to the tune of Rs.55,69,108. Being aggrieved of such disallowance, assessee preferred appeal before the first appellate authority. However, learned CIT(A) also confirmed the addition made by the A.O. Being aggrieved, assessee is in appeal before us.

20. The learned A.R. submitted before us that the assessee company has substantial reserves and the amounts advanced were out of such reserves and surplus and not out of interest bearing funds. It was submitted that even otherwise also the advances made were for the purpose of business. Explaining further, it was submitted that the amount of Rs.1,32,86,987 was advanced to M/s. KLR Mining and Equipments Ltd., which is a sister concern of the assessee. The said company went out of production but it has substantial plant and

machinery and sheds. The premises of the concern are within the same compound as that of the assessee. It was submitted that since the company is not in production, it has allowed the assessee to utilize its land, sheds and plant and machinery. The assessee also stood guarantee for some loans taken by the said company from bank. Therefore, if KLR Mining and Equipments Ltd., fails to meet its payment schedules, its assets will be put to auction by the Bank which will have serious repercussion on the business of the assessee company. It was submitted, to safeguard the interest of the assessee and its assets, the amount of Rs.1,32,86,987 was advanced to the said company. Therefore, it cannot be said that the investment made is not for business purpose. As far as investment made in Dubai is concerned, it was submitted that the assessee has opened a branch in Dubai to facilitate its entry into the markets of Middle-East by way of export. As far as investments in SBI-ONE India Fund and Palaka are concerned, it is submitted by the learned A.R. that the investments are out of own account and has no nexus with the borrowed fund. As far as advances made to Mr. Sanjay Kumar and Mrs. Rashmi Reddy is concerned, learned A.R. submitted the investment was for purchase of land and out of own account (surplus fund). The learned A.R. submitted that the A.O. has not disallowed any

interest on similar investment/advances made in assessment year 2008-2009. In support of its contention, the learned A.R. relied upon the decision of Hon'ble Supreme Court in the case of S.A. Builders 288 ITR (1) (S.C.). Thus it was submitted by the learned A.R. that disallowance of interest is not justified.

21. The learned D.R. on the other hand, supported the decision of the revenue authorities.

22. We have considered the submissions of the parties and perused the materials on record. The primary contention of the assessee is that the investments made are out of surplus fund and no interest bearing fund has been utilized. In our view, the aforesaid facts require verification since if there is no nexus between the investment made and the borrowed fund, then, no disallowance can be made. As these aspects are not examined by either A.O. or learned CIT(A), we are inclined to remit the matter back to the file of A.O. to verify and take a decision in the matter, after giving due opportunity of being heard to the assessee.

23. The next issue as raised in Ground No.5 of the revised ground as well as Ground Nos.6 and 8 of the additional ground are with regard to

disallowance made under section 40(a)(ia) of the Act.

24. Briefly the facts relating to this issue are, during the assessment proceeding, the A.O. noticed that the assessee has debited an amount of Rs.25,46,846 as interest on other loans, the details of which are as under :

Sl. No.	Particulars	Amount	Remarks
1.	Int. on vehicle loans Sundaram Finance & Sri Lekha Transportation	8,92,937	TDS not deducted
2.	Int. on car finance to various banks	3,78,909	---
3.	Ramireddy (Int. on loan)	12,00,000	TDS not deducted
4.	Prem Raj (Int. on loan)	75,000	TDS not deducted
	Total	25,46,846	

25. The A.O. was of the view that provisions of section 194A is applicable to such payments. Since the assessee has not deducted tax at source while making the payment, the A.O. disallowed an amount of Rs.21,67,937. However, the assessee out of the total disallowance made challenged the disallowance of Rs.8,92,937 only before the learned CIT(A). Before the first appellate authority, it was submitted by the assessee that since the payment was towards EMI of the hire purchase agreement

with M/s. Sundaram Finance Ltd., it will not come within the purview of section 194A of the Act. Learned CIT(A) after considering the submissions of the assessee and referring to CBDT Instruction No.1425 F.No.275/9/80-IT(B) dated 16.11.1981 directed the A.O. to re-examine assessee's claim.

26. The learned A.R. while challenging the disallowance of Rs.8,92,937 has also challenged the disallowance of Rs.3,78,909 being interest paid to banks Rs.12 lakhs being interest paid to Mr. Rami Reddy and Rs.75,000 to Mr. Premraj by raising additional ground. The learned A.R. submitted before us that as far as the amount paid to M/s. Sundaram Finance Limited towards vehicle loans is concerned, it is EMI paid under hire purchase agreement, hence, provisions of section 194A will not be applicable. He also submitted that provisions of section 194A will not be applicable to interest paid to banks amounting to Rs.3,78,909. It was also submitted by learned A.R. since the entire interest amount was paid during the relevant previous year and nothing remained payable, no disallowance under section 40(a)(ia) can be made in view of the decision of the ITAT, Vizag Special Bench in the case of Merlyn Shipping and Transport 146 TTJ (1).

27. The learned D.R. however, supported the disallowance of interest.

28. We have considered the submissions of the parties and perused the relevant materials available on record. The primary contention of the assessee is, since the entire interest amount is paid during the relevant previous year and nothing remained payable, no disallowance under section 40(a)(ia) can be made. We find merit in the aforesaid submissions of the assessee. As held by the ITAT, Vizag Special Bench in the case of Merylin Shipping and Transport (*supra*), no disallowance under section 40(a)(ia) can be made if the entire amount was paid during the relevant previous year and nothing remained payable. The Hon'ble Allahabad High Court also in case of CIT vs. Vector Shipping Services P. Ltd., 357 ITR 647 expressed similar view. Therefore, following the aforesaid decisions, we direct the A.O. to verify and allow the deduction claimed, if it is found that the entire amount was paid during the relevant previous year and nothing remained payable.

29. In ground No.7, assessee has challenged disallowance of an amount of Rs.53,58,187 as bad and doubtful debts written off.

30. We have considered the submissions of the parties and perused the relevant materials available on record. As could be seen the A.O. while completing the assessment, has disallowed

assessee's claim of bad and doubtful debts by observing that the assessee has failed to prove that the debt has become irrecoverable. However, on going through the provision of section 36(1)(vii) read with sub-section (2), it is very much clear that the only condition which are required to be satisfied are, it must have been shown as income in the earlier assessment year and it is actually written off in the books of account. There is no necessity on the part of the assessee to prove that the debt has become irrecoverable. Therefore, keeping in view the clear statutory provision, we direct the A.O. to verify these aspects and allow the deduction claimed by the assessee.

31. The next issue as raised in ground No.9 is with regard to disallowance of fee paid for increase of share capital amounting to Rs.3,01,452.

32. During the assessment proceeding, the A.O. noticed that the assessee has debited to the P & L account an amount of Rs.3,01,452 as fees paid to the ROC for increasing the authorized capital. The A.O. being of the view that expenditure incurred is in the nature of capital expenditure is not allowable. Accordingly, he disallowed the same. Assessee did not challenged the disallowance before the Ld. CIT(A) but has chosen to challenge the same before us through an additional ground. However,

on going through the facts and materials on record as well as principle of law on the issue, we agree with the view of the A.O. that the fee paid to ROC for increasing authorized share capital is a capital expenditure, hence, cannot be allowed. This ground is dismissed.

33. The next issue as raised in ground No.10 is, with regard to the disallowance of an amount of Rs.2,07,209 being employees contribution to ESI and PF.

34. The A.O. disallowed the expenditure claimed by observing that the assessee has not remitted the employees contribution to PF and ESI within the prescribed date as mentioned in section 36(1)(va). Though, the assessee did not challenge the disallowance before learned CIT(A) but he raised an additional ground before us challenging the said disallowance. It is the contention of the assessee that the employees contribution to ESI and PF though, was not paid within the due date as prescribed under section 36(1)(va) but such dues having been paid before the due date of filing of return of the income as prescribed under section 139(1), the amount is allowable as a deduction as per the provisions of section 43B. We find merit in the aforesaid submissions of the assessee. There are a number of judicial precedents on this issue

wherein it is held that if the employees contribution to PF and ESI is paid within the due date of filing of return of income under section 139(1), then, the amount is allowable as a deduction in view of the provision of section 43B. In view of the afore said, we delete the addition of Rs.2,07,209.

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

Order pronounced in the open Court on 15.07.2015.

Sd/-
(INTURI RAMA RAO)
ACCOUNTANT MEMBER

Sd/-
(SAKTIJIT DEY)
JUDICIAL MEMBER

Hyderabad, Dated 15th July, 2015

VBP/-

Copy to :

1.	KLR Industries Limited, Hyderabad. C/o. Mr. T. Chaitanya Kumar, Flat No.409, Metro Residency, Rajbhavan Road, Somajiguda, Hyderabad.
2.	DCIT, Central Circle 2(1), Hyderabad.
3.	CIT(A)-III, Hyderabad.
4.	CIT-II, Hyderabad
5.	D.R. ITAT 'A' Bench, Hyderabad.
6.	Guard File