

**IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCHES "A", BANGALORE**

Before Shri George George K, JM & Ms.Padmavathy S, AM

ITA No.721/Bang/2022 : Asst.Year 2016-2017

M/s.Rathod Developers & Builders, Captain Desai Park Narayanpur Dharwad - 580 008. PAN : AALFR7678E.	v.	The Income Tax Officer Ward 2(2) Hubli.
(Appellant)		(Respondent)

Appellant by : Sri.S.V.Ravishankar, Advocate
Respondent by : Sri.Gudimella V P Pavan Kumar, JCIT -DR

Date of Hearing : 19.10.2022	Date of Pronouncement : 02.11.2022
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ORDER

Per George George K, JM :

This appeal at the instance of the assessee is directed against CIT(A)'s order dated 20.06.2022. The relevant assessment year is 2016-2017.

2. The assessee has raised 15 grounds in its memorandum of appeal, however, the learned AR during the course of hearing had only argued the grounds pertaining to the following issues:-

(i) Whether additional income of Rs.2 crore declared during the course of survey can be treated as business profits and remuneration paid to partners on the same is to be allowed as deduction u/s 40(b) of the I.T.Act?

(ii) Whether the CIT(A) is justified in confirming the disallowance of Rs.3,31,868 being disallowance of 20% of Un-registered Dealer purchases (URD)?

We shall adjudicate the above issues as under:

Sum of Rs.2 crore declared during the course of survey, whether it pertains to business income or not? (Grounds 3 to 8)

3. The brief facts of the case are as follows:

The assessee is a partnership firm engaged in the business of construction of residential and commercial buildings. It also undertakes development of layouts. A survey u/s 133A of the I.T.Act was conducted on 22.12.2015 at the business premises of the assessee. A statement on oath was recorded from the partner of the assessee, Mr.Vimal Chand Pukhraj Telisara. During the course of survey, the Assessing Officer found a valuation report, wherein the cost of construction per square feet was mentioned at Rs.3,200, whereas the assessee had entered into sale agreement at an average rate of Rs.2,375 per sq.ft. The partner was confronted with the aforesaid valuation report. It was stated that the valuation report did not disclose the true and fair market value of the flat, however, the partner in order to buy peace with the Department, voluntarily offered a sum of Rs.2 crore as on-money received on account of 22 sale agreement, token advance for 14 flats and sale of open sites for the relevant assessment year 2016-2017. The assessee in the return of income for assessment year 2016-2017 disclosed a sum of Rs.2 crore in its profit and loss account. The assessee while arriving at the net profit of Rs.86,19,846.33 had claimed a deduction of Rs.1,31,54,770 towards partners remuneration as per section 40(b) of the I.T.Act.

4. The A.O. completed the assessment order u/s 143(3) of the I.T.Act (order dated 24.12.2028), wherein he held a sum of

Rs.2 crore declared during the course of survey cannot be treated as business receipts and had to be taxed u/s 115BBE of the I.T.Act. The A.O. worked out the allowance of remuneration to partners at Rs.11,54,770 on the basis of regular book profits at Rs.17,74,616 and disallowance balance remuneration claimed by the assessee. The A.O. also rejected the argument of the assessee that remuneration claimed by it would be taxable in the hands of the partners at the rate of 30% by observing that the partner had reduced their taxability by claiming various expenses against such income. The relevant finding of the A.O., for ready reference, reads as follows:-

5. On perusal of computation of income and P&L account of the assessee firm, it is seen that the assessee has declared gross sales of Rs. 4,65,92,700/- and declared gross profit of Rs. 10,75,199/-. Further, the assessee has declared Rs. 2,00,00,000/- as indirect income as admitted during the course of survey by its partner Shri VimalTelisara in his statement u/s 131(3) of the Income-tax Act, 1961 dated 22/12/2015. The assessee has considered the survey declaration of Rs. 2,00,00,000/- in his book profit as indirect income and debited partner's remuneration to the extent of Rs. 1,31,54,770/- on whole, which resulted into net profit of the firm as Rs. 86,19,846/- only. The assessee was asked to furnish the copy of partnership deed and working of remuneration excluding survey declaration of Rs. 2,00,00,000/-. The assessee, vide his submission dated 18.12.2018, has furnished the copy of partnership deed along with reworking of remuneration allowable to partners as below:

1. Net profit as per P&L account:	Rs. 86,19,846/-
2. Add: Remuneration paid to partner	Rs. 1,31,54,770/-
3. Less: Declaration under survey	Rs. 2,00,00,000/-
4. Book profit (i+ii-iii)	Rs. 17,74,616/-
5. Allowable remuneration as per IT Act-1961	Rs. 11,54,770/-
6. Net profit:	Rs. 6,19,846/-

- 5.1 The assessee, in his statement u/s 131(3) dated 22.12.2015, has voluntarily admitted Rs. 2,00,00,000/- additional income on account of 'on money', being difference of sell value and actual valuation report of flats at RT Enclave. The assessee has admitted Rs 800/- per square feet on money for total average constructed area of 25,000/- square feet in respect of 22 flats at RT enclave. Thereafter, the assessee has never disputed from his declaration or retracted from the statement u/s 131 (3) tendered by its partner,

since last two years. Further, he has declared his additional income of Rs. 2,00,00,000/- in his return of income for A.Y. 2016-17 as indirect income. During the course of Assessment proceedings, the assessee was given multiple opportunity but he never contended or disputed his additional income of Rs. 2,00,00,000/- declared during the course of survey. Therefore, the said income of Rs. 2,00,00,000/- can not be treated as regular book profit and the same is liable to be taxed u/s 115BBE. Thus, no remuneration or allowance is allowed against the survey declaration of Rs. 2,00,00,000/-.

The assessee was given opportunity vide notice u/s 142(1) dated 04.12.2018 before disallowance of remuneration paid to partner excluding survey declaration of Rs. 2,00,00,000/- on book profit. The assessee vide submission dated 12.12.2018 stated that *"all the partners are in 30% Bracket and there is no loss to the revenue by claiming remuneration from the declared income"*. The contention of the assessee is not acceptable as such in order to reduce tax liability of firm, the excess remuneration of Rs. 1.20 Crore has splitted in the hands of three partners. Further, the individual partners have set off their various expenses against remuneration so received. Thus, the straightway 30% tax liability on Rs. 1.20 Crore in the hand of assessee firm has been shifted and minimized by splitting the same as remunerations to the partner. Moreover, additional income of Rs. 2.00 Crore declared under survey can not be treated as regular book profit. The same is declared under survey on account of 'on money' receipt of sale consideration of flat which was not accounted in the books and is being taxed u/s 115BBE. Only Rs. 6,19,346/- is being assessed as regular business income after allowable remuneration of Rs. 11,54,770/- only, disallowing remuneration of Rs 1.20 crore.

Regular income: Rs. 6,19,346/-

Income u/s 115BBE: Rs. 2,00,00,000/-

5. Aggrieved by the order of the A.O., the assessee raised this issue before the first appellate authority. The CIT(A) rejected the contentions of the assessee by holding that there is nothing on record to suggest that a sum of Rs.2 crore surrendered by the assessee during the course of survey was its business income. The CIT(A) also distinguished the case laws relied on by the assessee. The CIT(A) held that there was a factual finding in those cases relied on, wherein the additional income was treated as from business only.

6. Aggrieved by the order of the CIT(A), the assessee has raised this issue before the Tribunal. The learned AR filed a paper book comprising of 121 pages, enclosing therein the computation of income, acknowledgement for the return filed, copies of the financial statements for the relevant assessment year in the case of the assessee as well as its partners, statement on oath taken from the partners, copies of the notices and replies submitted, etc. The learned AR submitted that the partner of the assessee in the sworn statement recorded at the time of survey dated 21.12.2015 had offered additional income of Rs.2 crore, which is nothing but business income arising out of the construction activities undertaken by the assessee. It was contended that the valuation arrived in the cost of construction is as per the industrial standards and there is no infirmity in the books of account of the assessee. It was contended that the possibility of receiving additional income due to the increase in the rate of construction cannot be ruled out in future years and it is in this context, a sum of Rs.2 crore was disclosed. Therefore, it is submitted that the same is to be treated as business income and no inference could be drawn that additional income was unexplained. It is further submitted that there was no cash or incriminating documents found in the premises of the assessee to draw inference that there was unexplained receipts in the nature of income warranting invocation of section 115BBE of the I.T.Act. Further, it was contended that there was no loss to the Revenue, since the partners salary has been taxed at the maximum marginal rate. Lastly, it was contended that the partners salary was a

mandatory charge on the profits and a permissible deduction u/s 40(b)(v) of the I.T.Act. In other words, it was contended that the additional income once it is treated as business income, the natural consequences in arriving at the total taxable income is after allowing deduction of remuneration paid to the partners u/s 40(b)(v) of the I.T.Act. In this context, the learned AR relied on the judgment of the Hon'ble jurisdictional High Court in the case of CIT v. S.K.Srigiri & Bros reported in 298 ITR 13 (Kar.).

7. The learned DR supported the order of the A.O. and the CIT(A). It was submitted that the additional income offered of Rs.2 crore is not a business income and the same has been rightly taxed as per the provisions of section 115BBE of the I.T.Act. Therefore, it was stated that the A.O's order, which was confirmed by the CIT(A) in not granting deduction u/s 40(b)(v) of the I.T.Act in respect of excess remuneration is correct and no interference is called for.

8. We have heard rival submissions and perused the material on record. The sworn statement of the partner is placed on record at page 26 and 27 of the paper book filed by the assessee. The relevant question and answer to the same, namely, question No.8 and its answer, reads as follows:-

“Q.8 : There is a difference of about Rs.800/- per sq.ft. for the 22 apartments (25,000 sq.ft) wherein sale agreements have been made and the valuation report found. Please explain.

Ans. : The valuation report was given by the customer who does not reflect the correct rate per sq.ft. However, I am voluntarily offering a sum of Rs.2 crores as on money received on account of the 22 sale agreements made as well as token

advance received for the balance 14 flats & sale of open sites for the A.Y. 2016-17.”

9. From the above answer to question No.8, it is clear that the additional income has been offered on account of sale of flats. The undisputed fact is that the assessee is in the business of construction of flats, commercial buildings, and undertakes development of layouts. The additional income has been disclosed on account of amounts received from the customers towards future sale of flats and open sites. Further, from the above answer, it is clear that the rate itself stated by the A.O. during the course of survey is in respect of valuation report obtained by the prospective buyers and not from the assessee. Therefore, for all practical purposes, same is likely to be inflated for obtaining loans from financial institution and could not be construed to be price of the units accruing to the assessee. It is further to be noticed that the survey u/s 133A of the I.T.Act was conducted on 22.12.2015 and the assessment year under consideration, i.e., A.Y. 2016-2017, was not complete. The manner of computation by the assessee in arriving at the additional income of Rs.2 crore as per the sworn statement demonstrate that it is directly relatable to the construction of flats, and hence, deem to accrue as part of the consideration of sale of flats and thus the income is to be treated as income from business of the assessee. The surrendered income disclosed by the assessee are part of the business activities and as mentioned earlier no other activities were carried on by the assessee, nor has the Revenue brought on record any contrary material for the aforesaid conclusion. Moreover, the Revenue has not found

any money during the course of survey. Further, the tax rate specified u/s 115BBE of the I.T.Act for assessment year 2016-2017 is at 30% (same as the normal rate) and the partners of the assessee after considering the remuneration have discharged tax liability more or less at the same rate of 30%. Thus, we are of the view that there is no loss to the revenue. The average tax rate of the partners for the relevant assessment year are detailed below:-

Particulars	Raju B Jain	Vimalchand T Telisara	Mahendra B. Rathod
Taxable income (A)	1,24,15,030	49,63,000	49,09,700
Total Taxes paid (B)	48,29,216	14,86,423	15,08,462
Average Tax Rate (A/B)*100	38.90%	29.95%	30.72%

10. Based on the above working, it is clear that the partners have paid average tax at 30%. Therefore, the observation of the A.O. at para 5.2 at page 3 of the impugned assessment order that *“individual partners have set off their various expenses against remuneration so received. Thus, the straightway 30% tax liability on Rs.1.2 crore in the hand of assessee firm has been shifted and minimized by splitting the same remuneration to the partner”* is factually incorrect.

11. As regards the allowability of remuneration of Rs.1,20,00,000 in the hands of the partners is concerned, there is no dispute as regards the entitlement of the remuneration by the partners, since the A.O. had allowed the remuneration as per section 40(b)(v) of the I.T.Act to the extent of Rs.11,54,770. The dispute is with regard to whether the assessee is entitled to remuneration as per section 40(b)(v)

of the I.T.Act on the additional income offered. Since we have already held that the additional income offered by the assessee is to be considered as business income, as a natural corollary, the remuneration u/s 40(b)(v) of the I.T.Act has to be computed considering the entire business income declared by the assessee. In this context, we rely on the judgment of the Hon'ble jurisdictional High Court in the case of CIT v. S.K.Srigiri & Bros reported in 298 ITR 13 (Kar.). The relevant finding of the Hon'ble jurisdictional High Court reads as follows:-

“5. We have perused the orders of the Tribunal. The Tribunal has carefully considered the questions put by the authority and the answer of the partners of the assessee's firm and based on the same, the Tribunal has come to the conclusion that the additional income received by the assessee in the instant case is from business and not from other sources. If the Tribunal has come to the conclusion that the additional income is from business, the remuneration paid to the partners has to be deducted while considering the profit and loss. In the circumstances, we are of the opinion that on facts the revenue has no case on the merits. So far as the question of law is concerned, we have to answer the same in favour of the revenue.

6. Hence, these appeals deserve to be dismissed by upholding the orders passed by the Income-tax Appellate Tribunal and they are dismissed.”

12. The facts of the instant case are similar to the judgment rendered by the Hon'ble jurisdictional High Court (supra). Since we have held that the additional income offered as part of the business income, the assessee would be entitled to deduction as per the provisions of section 40(b)(v) of the I.T.Act. It is ordered accordingly.

13. Hence, grounds 3 to 8 are allowed.

URD Purchases (Grounds 11 to 13)

14. The A.O. in the assessment completed, had disallowed on adhoc basis, a sum of Rs.3,31,868 being 20% of the URD purchases amounting to Rs.16,59,344. The view taken by the A.O. was confirmed by the CIT(A). The relevant finding of the CIT(A) reads as follows:-

“9.1. The report of the AO was duly confronted to the appellant. In response to the same the appellant has submitted that the disallowance is excessive and that the same be reduced to 10% of the URD purchases. The submissions of the appellant and report of the AO have duly been considered. The appellant has not substantiated its argument to support its claim. The purchases are unverifiable and in cash. So the action of the AO in disallowing 20% of the same cannot be considered as unreasonable. The action of the AO is upheld and the ground of appeal 8 is dismissed.”

15. Aggrieved, the assessee has raised this issue before the Tribunal. The learned AR submitted that the disallowance of URD purchases was never raised or discussed in any of the statutory notices issued u/s 142(1) of the I.T.Act. Therefore, there was a violation of principle of natural justice. Further, it was contended that the unregistered dealers are small scale businessmen, who trade in jelly, stones, bricks etc. It was stated that these businessmen do not possess any VAT registration. It was stated that the URD purchases forms a miniscule portion of the total purchases, which amounts to only 2% of the total purchases.

16. The learned DR supported the orders of the A.O. and the CIT(A).

17. We have heard rival submissions and perused the material on record. Undisputedly, the URD purchases are only 2% of the total purchases. Considering the nature of the assessee's business, i.e., the construction of flats and commercial buildings, undoubtedly, the assessee has to make purchases, such as jelly, stones and bricks etc. In the facts and circumstances of the case, we are of the view that the adhod disallowance at the rate of 20% of the URD purchases is highly excessive. The assessee itself before the first appellate authority stated that the disallowance at 20% is excessive and should be reduced to 10% of the URD purchases. Accordingly, we limit the disallowance of URD purchases to 10% of Rs.16,59,344. Hence, we sustain an addition of Rs.1,65,934 and delete the balance. It is ordered accordingly.

18. Hence, grounds 11 to 13 are partly allowed.

19. In the result, the appeal filed by the assessee is partly allowed.

Order pronounced on this 02nd day of November, 2022.

Sd/-
(Padmavathy S)
ACCOUNTANT MEMBER

Sd/-
(George George K)
JUDICIAL MEMBER

Bangalore; Dated : 02nd November, 2022.
Devadas G*

Copy to :

1. The Appellant.
2. The Respondent.
3. The CIT(A)-11, Bangalore.
4. The Pr.CIT (Central), Bangalore.
5. The DR, ITAT, Bengaluru.
6. Guard File.

Asst.Registrar/ITAT, Bangalore