

**IN THE INCOME TAX APPELLATE TRIBUNAL
DIVISION BENCH 'A', CHANDIGARH**

BEFORE SHRI SANJAY GARG, JUDICIAL MEMBER
AND MS. ANNAPURNA GUPTA, ACCOUNTANT MEMBER

ITA No.463/Chd/2016
(Assessment Year : 2009-10)

M/s A.P. Refinery (P) Ltd.,
Village Saroud, Ludhiana Road,
Malerkotla.
(Now Village Tappar Harnia,
Nakodar Jalandhar Road,
Jagraon)
PAN: AAFCA1352B
(Appellant)

Vs.

The Income Tax Officer,
Ward-4(3),
Malerkotla.

(Respondent)

Appellant by : Shri Ashwani Kumar

Respondent by : Smt.Zeenia Handa, Addl. CIT DR

Date of hearing :05.10.2017

Date of Pronouncement :30.10.2017

ORDER

PER ANNAPURNA GUPTA, A.M.:

This appeal filed by the assessee is directed against the order of learned Commissioner of Income Tax(Appeals)-2, Ludhiana (hereinafter referred to as 'CIT(Appeals)' dated 26.2.2016 relating to assessment year 2009-10.

2. Ground No.1 raised by the assessee reads as under:

"1. That order passed u/s 250(6) of the Income Tax Act, 1961 by the Ld. Commissioner of Income Tax (Appeals)-S, Ludhiana is against law and facts on the file in as much she was not justified to arbitrarily uphold the disallowance of Rs. 2,24,340/- on account of under-valuation of closing stock of husk."

3. Brief facts are that during the course of assessment proceedings, the Assessing Officer observed that the assessee had 22,434 quintals of husk in the closing stock

which were valued by the assessee at average price. The Assessing Officer further observed that the assessee had purchased husk at rates which ranged between Rs.148 to Rs. 154 per quintal in the months of Feb and March, 2009. The Assessing Officer also observed that the assessee had also shown purchase of phoosa @ Rs.110 per quintal but the supporting bills/vouchers of the same were undated and did not bear any number. The Assessing Officer therefore took the average cost price of husk at Rs.150 and difference of Rs.10, as observed by the Assessing Officer, between actual valuation done by the assessee and that done him, was added to the value of closing stock. Therefore, the Assessing Officer made addition of Rs.2,24,340/- (Rs.22,434 x 10) on account of under valuation of closing stock.

4. Before the Ld.CIT(Appeals), the assessee made detailed submissions reproduced at para 5.2 of the order stating that it had valued the closing stock of rice husk at average rate of purchase which method was being consistently followed by it every year and details of the same had also been filed to the Assessing Officer. The Ld.CIT(Appeals) rejected submissions of the assessee and upheld the addition made by the Assessing Officer stating as under:

“5.3 I have carefully considered rival submissions. I am inclined to agree with the contention of Id. AO. The assessing officer has brought out the basis of adoption of closing stock valuation in which the appellant has failed to controvert. The appellant has not controverted the inference of Id. AO with the support of bills and vouchers and the basis of its valuation shown by the appellant. Therefore in my

considered view the action of Id. AO. Is right. The appellant has failed to furnish any plausible contention in support of low valuation of closing stock with production of related bills and vouchers. Therefore, the addition on account of valuation of closing stock is ordered to be confirmed. This ground of appeal is dismissed.”

5. Before us, the Ld.Counsel for the assessee reiterated the contentions made before the lower authorities stating that it had been consistently following method of valuation of closing stock of husk at the yearly average of purchase price of the same. The Ld. counsel for assessee drew our attention to the details of the calculation of the same for both the units run by the assessee filed before the lower authorities and placed at Paper Book page Nos. 12 & 13. The Ld. counsel for assessee stated that in view of the same, there was no reason to disturb the method following consistently by the assessee.

6. The Ld. DR, on the other hand, relied upon the order of the lower authorities.

7. We have heard contentions of both the parties, perused the orders of authorities below and also gone through the documents placed before us. We find merit in the contention of the Ld. counsel for assessee. The assessee has all along contended that it has been consistently following the average cost method of valuing its closing stock. Details with regard to the valuation for the impugned year were also filed to the Assessing Officer. These facts remain uncontroverted by the Revenue. Further we find that no fault has been found in this method of valuation vis-à-vis determination of the true

and correct profits of the assessee. Therefore, any disturbance or change in the system/method of valuation was totally unwarranted. Further no reason has been given for adopting the average rate of purchase of last two months for valuing the closing stock. Therefore, this method of valuation adopted by the Revenue needs to be rejected. Further, we find that the Revenue has contended that the assessee has shown purchase of phoosa @ Rs.110 per quintal which bills were found undated and unnumbered meaning thereby that they were bogus. But at the same time, we find that no disallowance of purchase booked on account of such bills has been made. Therefore, there is no merit in the contention of the Revenue that the stock has been undervalued deliberately by the assessee.

Therefore, for the above reasons, we hold that the addition made on account of under valuation of stock amounting to Rs.2,24,340/- be deleted.

Ground of appeal No.1 raised by the assessee, therefore, stands allowed.

8. Ground of appeal No.2 (a) raised by the assessee reads as under:

2. That the Ld. CIT(A) was further not justified to arbitrarily uphold the disallowance of interest u/s 36(1)(iii) on the following:-

a) Rs. 36,85,302/- on account of interest required to be capitalized;

9. Brief facts are that during the course of assessment proceedings, the Assessing Officer noted that the assessee

had debited Rs.84,89,380.43 as interest and financial charges. The Assessing Officer observed that the assessee had started the Unit-II during the year and as such had availed finance from the banks and by way of unsecured loans. The Assessing Officer asked the assessee to explain that why proportionate interest should not be added back because production started only on 19.02.2009. In his reply the assessee submitted the details of interest separately for the two units i.e. Unit-1 (old unit) and Unit-II (new unit). From the perusal of accounts the Assessing Officer observed that the assessee had wrongly claimed certain amounts of interest and processing charges in the Unit-1, the Assessing Officer further observed that Unit-1 was on lease during the year under consideration, hence, the Assessing Officer did not accept the investment in this unit. The Assessing Officer was of the view that the assessee had not fully capitalized the relevant amount. Therefore, amount of interest which ought be disallowed and be capitalized was calculated by the Assessing Officer as follows:

A. Out of Interest Bank A/C Rs. 491621.50. interest debited in the accounts PNB CC A/c 3881008700002843 and PNB CC A/C 3881008700002852 as above upto 19.02.200 are calculated at Rs.2243650.

B. Out of Interest (T/L) A/c Rs. 1385462,52, interest debited in the accounts PNB T/L A/c 3881 00i.C0000109 as above & ICICI T/L upto 19.02.2009 is calculated at Rs.1225857.00

C. Out of total amount of Processing Fees Rs.288525.48 Rs.215795.48 debited before 19.02.2009, as it pertains to the processing charges levied by the bank in relation to new loan and CC accounts raised during the year in relation to Unit-2.

As such total amount of Rs.36,85,302.00
[Rs.2243650.00 + Rs.1225857.00 + Rs.215795.00] was

disallowed from the interest and financial charges as calculated above and added back to the returned income.

10. Before the Ld.CIT(Appeals) the assessee made detailed submissions reproduced at para 7.2 of the order contending that there was no need for capitalization of any interest towards the setting up of unit-II by assessee since the assessee had on its own capitalized interest amounting to Rs.37,65,517/- which was much more than the amount capitalized by the AO of Rs.36,85,302/-. It was contended that separate details of interest pertaining to unit-I and unit-II of the assessee had been filed to the Assessing Officer and the Assessing Officer had capitalized the interest incurred on account of unit-1 which was already in commercial production and was an old unit. The assessee pointed out that in unit-I the assessee company had been dealing with Punjab & Sind Bank as well as ICICI bank in respect of credit facilities but on the setting up of unit-II it got credit facilities from Punjab National Bank which took over existing limits from other two banks also. The assessee pointed out that in this confusion that Punjab National Bank Limited pertains to unit-II the Assessing Officer had capitalized the amount of interest in respect of facilities availed by unit-I also. The assessee further submitted that processing charges were all entirely paid in respect of unit-I only. The Ld.CIT(Appeals) dismissed contentions and submissions made by the assessee and

upheld the findings of the Assessing Officer by stating as under:

“7.3 I have carefully considered rival submission. While going into detailed submission by appellant and the assessment order, I am inclined to agree with the contention of the AO. The AO has pointed out that production started only on 19.02.2009. From the perusal of accounts the AO observed that the appellant had wrongly claimed the certain amounts of interest and processing charges in the Unit-I. The AO further observed that Unit-I was on lease during the year under consideration, hence, the AO did not accept the investment in this unit. In view of the facts of the case I agree with the view of the AO that the appellant had not fully capitalized the relevant amount.”

11. Before us, the Ld. counsel for assessee reiterated submissions made before the lower authorities drawing our attention to the relevant details of interest paid vis-à-vis of two units filed at page No.15-18 of the Paper Book.

12. The Ld. DR, on the other hand relied upon the order of the Assessing Officer.

13. We have heard contentions of both the parties, perused the orders of authorities below and also gone through the documents placed before us. We find that the entire exercise of the Revenue of capitalizing interest expenditure rests on the premise that no interest expenses vis-à-vis setting up of unit-II was capitalized by the assessee. The assessment order finds no mention of this fact.

Even the Ld.CIT(Appeals), we find, has not taken cognizance of this averment made by the assessee. Therefore, considering the fact that the assessee had itself capitalized an amount of Rs.37,65,517/- which is more than

what the Revenue has calculated at Rs.36,85,302/-, we hold that there is no need for capitalization of any further amount. Moreover, we find that the contention of the assessee that separate details of interest charged vis-à-vis unit-I and unit-II were filed and it was only interest paid vis-à-vis pertaining to unit-I which was capitalized by the Assessing Officer has not been controverted by the Revenue. Undeniably the AO has capitalized interest pertaining to PNB CC A/c, PNB T/L a/c and out of processing fees levied by bank in relation to new loan and CC accounts. The assessee had stated that these loans did not pertain to Unit-II, but in fact to Unit-I loans only which were originally taken from Punjab & Sind bank but later shifted to PNB bank and since the loans in Unit II had been taken from PNB the AO had confused these loans as pertaining to Unit-II. The processing charges were also stated to be vis-a-vis the conversion of the aforesaid loans. The revenue has not controverted these facts. Therefore there remains no basis at all for holding that these loans pertained to Unit II. No disallowance of interest was therefore warranted in the above set of facts.

In view of the above we delete the disallowance of interest amounting to Rs.36,85,302/-.

Ground of appeal no.2(a) therefore stands allowed.

14. Ground No.2(b) raised by the assessee reads as under:

b) Rs. 2,81,500/- on account of interest-free non-business advances.

15. Brief facts are that during the course of assessment proceedings, the Assessing Officer noted that the assessee had given interest free loan to its sister concern M/s A.P. Solvex Ltd., Dhuri on 11.10.2008. The assessee was asked as to why proportionate interest for 50 lacs for the period 11.10.2008 to 25.02.2009 at the average rate of 15% should not be disallowed. The Assessing Officer was not satisfied with the assessee contention. Therefore interest was charged @15 on average basis from 11.10.2008 to 25.02.2009 which came to Rs.2,81,500/- and was disallowed by the Assessing Officer. The Assessing Officer placed reliance the decision of Punjab & Haynana High Court in the case of CIT vs. Abhishek Industries Ltd.

16. The Ld.CIT(Appeals) dismissed the ground raised before it and upheld the order of the Assessing Officer stating that the commercial expediency of giving the advance was not established by the assessee.

17. Before us, the only contention raised by Ld. counsel for assessee was that it had enough own surplus funds to make the impugned advance. The Ld. counsel for assessee drew our attention to the Balance Sheet of the assessee stating that it had own interest free funds in the shape of capital reserves and surplus and share application money amounting to Rs.10.68 crores, while the advance given amounted to Rs.50 lacs. The Ld. counsel for assessee pointed out that the law on the issue of disallowance u/s 36(1)(iii) of the Act has been settled by the Hon'ble

jurisdictional High Court in a number of decisions wherein it has been stated that where the assessee had sufficient own interest free funds for making interest free advances, no disallowance u/s 36(1)(iii) of the Act is warranted.

18. The Ld. DR, on the other hand, relied upon the order of the lower authorities and stated that in the absence of any commercial expediency having been established for making said advances, disallowance u/s 36(1)(iii) of the Act had been rightly made.

19. We have heard the contentions of both the parties. We find merit in the contention of the Ld. counsel for assessee. Undoubtedly, the Hon'ble jurisdictional High Court in the case of Bright Enterprises vs CIT (2016) 381 ITR 107, has stated that in the fact situation of availability of interest free funds for the purpose of making interest free advances the presumption should be that the said advances had been made out of own interest free funds warranting no disallowance u/s 36(1)(iii) of the Act.

20. In the present case, it had been demonstrated by the Ld. counsel for assessee that it had sufficient interest free funds to make the said advances which have not been controverted by the Ld. DR.

In view of the same and following the judicial precedent this regard, we hold that no disallowance u/s 36(1)(iii) of the Act is warranted in the present case and

thereby direct to delete the disallowance so made amounting to Rs.2,81,500/-.

Ground No.2(b) raised by the assessee, therefore, stands allowed.

21. In view of the above, the appeal of the assessee stands allowed.

Order pronounced in the open court.

Sd/-

Sd/-

(SANJAY GARG)
JUDICIAL MEMBER

(ANNAPURNA GUPTA)
ACCOUNTANT MEMBER

Dated : 30th October, 2017

Rati

Copy to:

1. The Appellant
2. The Respondent
3. The CIT(A)s
4. The CIT
5. The DR

Assistant Registrar,
ITAT, Chandigarh