AOs cannot make ad-hoc additions without going into details. Assesses also cannot claim expenses without showing commercial expediency. However, AOs thereafter cannot question pure business decisions [Sec 37 & 40A(2) of ITA'61 – Sec 34 & 35 of ITA'25]

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Upteen no:of times during assessments it is seen that AOs have made additions by disallowing purchases and the same is accepted by assesses. However, it is a good development that even SME businesses are now fighting for their rights. AOs have to now earn every bit of tax rightfully without resorting to ad-hoc deductions as New India's MSME's become more organized and have evidences and vouchers to substantiate their expenses and purchases. ITAT Kolkata has passed a judgement in the case of SANJAY TRANSPORT AGENCY Vs ACIT, CIRCLE-3(1), ASANSOL [2023-VIL-437-ITAT-KOL] which may not be very significant as far as jurisprudence is concerned but reflects on the new business environment. In this case, In course of appellate proceedings before CIT(A), assessee had given complete details of expenditure on spare parts as well as machines purchased for purpose of carrying out contractual work. CIT(A) did not doubt genuineness of type of expenditure incurred by assessee, but sustained disallowance @20% without finding any specific defect in these details. It was held that Disallowance made by CIT(A) is merely ad hoc in nature. Sales/gross receipts are not disputed at any stage and for achieving the same, it was held that the assessee needs to incur expenditure. It was held that the AO was not justified in making additions towards bogus expenditure. CIT(A) has erred in sustaining addition by making ad hoc disallowance without specifying any defect in books of accounts and records maintained by assessee. Order passed by CIT(A) was thus set aside.

However, there is counter department's dimension also. It is important to assesses also to show business purpose and commercial expediency for every expenditure and expenses will not be allowed merely because bills are there and payment has been made by Bank Account. Expecially incase of trading firms it is seen that huge charge of business promotion expenses are there sometimes. It has to be substantiated that how these business promotion expenses actually led to or atleast was considered to lead to proportionate increase in business. It was held in the case of SRI DINESH DEVRAJ RANKA Vs THE ADDITIONAL COMMISSIONER OF INCOME TAX [2023-VIL-401-ITAT-BLR] that mere assertion that expenditure was incurred for promoting business cannot be accepted without establishing nexus between expenditure and business. However, in interest of justice, the matter was remitted back to CIT(A) to examine issue afresh based on evidences that the assessee may submit in this regard. In the same matter claim of assessee in regard to amount paid towards property advance, not supported by any documents which AO called for during assessment proceedings - not substantiated, Amount written off against salary advance - not substantiated and Claim of bad debts - not substantiated with proper documentary evidence to prove that it is incurred in regular course of business and amount could not be recovered, were all disallowed by The Hon'ble Tribunal.

However, once the business expediency is shown, and there is no related party transaction involved within meaning of Section 40A(2) of the Income Tax Act, then the ALP cannot be disputed. AO cannot step into the shoes of a businessman and interfere with the business decision of assessee. The same was held by the ITAT-Kolkata in the case of ASSISTANT COMMISSIONER OF INCOME TAX, CIRCLE-11(2), KOLKATA Vs SAFAL PROPERTIES PVT LTD [2023-VIL-414-ITAT-KOL]. Here the interest charged by one party @16% instead of 10% was disputed as an exorbitant rate.

LET'S DISCUSS FURTHER!

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