IN THE INCOME TAX APPELLATE TRIBUNAL
*KOLKATA BENCH "**C**" KOLKATA*

Before **Shri N.V.Vasusdevan, Judicial Member** and
Shri Waseem Ahmed, Accountant Member

ITA No.1754/Kol/2013 Assessment Year :2009-10

Surovi Mansion Jewellers Pvt. Ltd. 195/13B, Rash Behari Avenue, Kolkata-700 019 [**Pan No.AAICS 3050P**]	**V/s**.	The Income Tax Officer, Ward-12(1), 3, Govt. Place, Kolkata-700 001
अपीलार्थी /Appellant	..	प्रत्यर्थी/Respondent

अपीलार्थी की ओर से/By Appellant	Shri A.K.Tibrawal, FCA
प्रत्यर्थी की ओर से/By Respondent	Shri Pinaki Mukherjee, JCIT-DR
सुनवाई की तारीख/Date of Hearing	16-03-2016
घोषणा की तारीख/Date of Pronouncement	13-04-2016

आदेश /O R D E R

PER Waseem Ahmed, Accountant Member:-

This appeal by the assessee is arising out of order of Commissioner of Income Tax (Appeals)-XII, Kolkata dated 22.03.2013. Assessment was framed by ITO Ward-12(1), Kolkata u/s 115WE(3) of the Income Tax Act, 1961 (hereinafter referred to as 'the Act') vide his order dated 30.12.2011 for assessment year 2009-10.

2. First issue raised by assessee is that Ld. CIT(A) erred in confirming the action of Assessing Officer by disallowing a sum of ₹28,69,878/-. The effective ground is reproduced below:-

> *"1) That the Learned Commissioner of Income Tax (Appeals) erred in confirming the disallowance of Rs.28,69,879, made by the Assessing Officer,*

under section 40A(3) of the Income Tax Act, 1961, when actual cash payments never exceeded the sum of Rs.20,000 on any date whatsoever."

3. Brief facts as culled out from the record are that assessee is a Private Limited Company and engaged in the business of manufacturing and retailing of gold & silver ornaments and precious and semi precious stones. The assessee filed its return of income on 30-09-2009 declaring total income of ₹2,13,930/- under the head " business & profession". However, AO framed u/s 143(3) of the Act by assessing the income of assessee at ₹34,40,850/-.

It was submitted that when customers exchanged their old ornaments in place of new ornaments then assessee accounts for purchase and sale of the ornaments simultaneously. The difference between purchase & sale value is settled either by cash or account payee cheque. In such a situation, assessee issued two invoices – one for purchase of ornaments and other one for sale of ornaments. Similarly, assessee records the payment transactions against the purchase and receipt transactions against the sale of ornaments in the cash book. However, in the actuality the transaction will only be settled with the customer at the amount of the difference arising between purchase and sale value of ornaments. The AO on examining the cash book found that payment for old gold purchase account exceeds ₹20,000/- and as such it violates the provisions of section 40A(3) of the Act. The plea of the assessee that the transaction of purchase and sale of the ornaments should be verified in the context of net of purchase-sales was disregarded by the AO. During the assessment proceedings, AO found that the assessee has made purchase of ornaments exceeding the payment of ₹20,000/- which aggregates to Rs. 28,69,878/-. The AO also observed that such transaction is also not falling under any of the exception category as specified in rule 6DD of Income Tax Rules 1962 and finally disallowed a sum of ₹28,69,878/- for the violation of the provisions of section 40A(3) of the Act and added to the total income of the assessee.

4. Aggrieved, assessee preferred an appeal to learned CIT(A) who confirmed the action of AO by observing that the additions was made for the violation of section 40A(3) of the Act on account of the payment for purchase of old ornaments exceeding Rs. 20,000/-. Accordingly the plea of assessee was rejected that the aforesaid disallowance relates to the transactions of purchase of old ornaments in exchange of new ornaments and transaction of purchase of old ornaments should be viewed in the context of net figure of purchase and sale.

Being aggrieved by this order of Ld CIT(A) assessee is in second appeal before us.

5. We have heard rival contentions of both the parties and perused the materials available on record. Before us ld. AR filed a paper book which is running from page 1 to 87 and drew our attention on pages 1 & 2 of the paper book where the details of the parties to whom new ornaments were sold in exchange of old ornaments along with net amount adjusted with the parties. In none of the case the net payment was exceeding for the purchase of the old ornaments beyond ₹20,000/-. Although the assessee on sale of new ornaments in exchange of old ornaments was reflecting the transaction as independent purchase and sale in the books of accounts but in actuality the party account was adjusted with the net amount. For example, Mr. S. Bhattacharjee sold old gold to the assessee and the assessee issued the purchase memo which is placed on record on page 3 of the paper book. The value of the purchase of the old gold was ₹ 20,890/- and the same was shown as payment to the party in the cash book on page 45 of the paper book. The assessee sold new gold for Rs. 20,725.00 to the aforesaid party on dated 26/10/2008 vide sale memo no. 8CM/1547 which is placed on page 4 of the paper book. The same sale was shown as receipt in the cash book on page 42 of the paper book. But in actuality in the instant case only the difference amount of Rs.165.00 (sale price Rs. 20,725/- purchase price Rs. 20,890/-)

was paid to the aforesaid party. However, in the cash book both purchase & sale were recorded at the full value. The assessee also submitted that wherever the payment exceeds ₹20,000 then the payment was made by way of account payee cheque only. Besides the above, assessee further submitted that the above process of payments are permitted in terms of clause (d) of rule 6DD of Income Tax Rules. On the other hand, ld. DR vehemently supported the order of lower authorities.

5.1 From the aforesaid discussion, we find that the AO has invoked the provisions of section 40A(3) of the Act on the ground that assessee has made the payment in cash exceeding ₹20,000 for the purchase of old ornaments and the same was confirmed by the Ld CIT(A). However, from the facts of the case and submission of the assessee, we find that in none of the case the payment is exceeding ₹20,000 for the purchase of old ornaments. In all the cases where the addition was made by the AO on account of deemed payment of ₹20,000 on the purchase of old ornaments, the assessee sold ornaments in exchange thereof. As a result, the net payment was made the party for the purchase of old ornaments. However the assessee in its books of accounts was showing purchase and sale in full value and the same was also recorded as payment for the purchase and receipt for the sale in the cash book. In our considered view merely recording the connected purchase and sale transactions independently and separately instead of net adjusted amount in the cash book does not amount the violation of section 40A(3) of the Act. On examination of record of the net amount of purchase and sale of the ornaments we did not find even a single case where the payment is exceeding ₹20,000. However we find that wherever the payment exceeds for purchase more than ₹20,000, it has been made through account payee cheque only as evident from the submission of the assessee which is placed on page number 1 and 2 of the paper book. The Ld DR also failed to bring anything corroborative evidence on record to controvert the arguments of the ld. AR. In addition to the above, we also find that an exception in clause (d) to

Rule 6DD of Income Tax Rules 1962 has been provided which reads as under:-

> *"(d) where the payment is made by way of adjustment against the amount of any liability incurred by the payee for any goods supplied or services rendered by the assessee to such payee."*

In view of the above, we conclude that the assessee has not violated provisions of section 40A(3) of the Act on account of payment exceeding for the purchase of old ornaments exceeding ₹20,000. Accordingly, we reverse the orders of lower authorities and this ground of appeal of the assessee is allowed.

6. Second issue raised by assessee in this appeal is that ld. CIT(A) erred in confirming the order of AO by disallowing a sum of ₹2,53,243/- under section 40(a)(ia) of the Act considering the melting loss incurred by KARIGARS is nothing but payment made to KARIGARS without deducting TDS. For this, assessee has raised effective ground as under:-

> *"2) That the Learned Commissioner of Income Tax (Appeals) erred in confirming the disallowance of Rs.2,53,243 made arbitrarily by the Assessing Officer under section 40(a)(ia) of the Income Tax Act, 1961 on the alleged ground that the melting loss incurred by karigars is, actually, amount paid to them without deducting tax at source."*

7. The assessee hired the services of KARGARS for the making of ornaments. During the year, assessee in some cases received the lesser weight of gold from the KARIGARS and those KARIGARS were either paid lesser or no amount for their services. Accordingly the AO opined that the payment to those KARIGARS has been paid in the form of the gold. The assessee submitted that the lesser gold was received due to loss of gold in manufacturing process which is bound to happen and the same loss is also recognized in Foreign Trade Policy to the extent of 3.5% as wastage. Accordingly, the assessee submitted the working of such loss of 906.880 grams with reconciliation but failed to reconcile such loss to the extent of

166.170 grams. Accordingly the AO opined that the loss on making of ornaments to the extent of 166.170 grams represents the payments to KARIGARS in the form of gold as it is excess gold left with them in lieu of making charges. The AO further opined that this payment had been made in the form of gold without deducting TDS under section 194C of the Act. Therefore it was disallowed under section 40(a)(ia) of the Act. Accordingly the AO made an addition of Rs. 2,53,243.00 (166.170 X Rs. 1524) to the total income of the assessee.

8. Aggrieved, assessee preferred an appeal to ld. CIT(A) who confirmed the action of AO by observing that the loss to the extent of 3.5% was accepted in terms of foreign trade policy as melting and manufacturing loss. The loss more than 3.5% was disallowed due to non-availability of reconciliation statement.

Being aggrieved by this order of Ld CIT(A) assessee is in second appeal before us.

9. We have heard rival contentions and perused the materials available on record. Before us Ld. AR submitted that as per the understanding with the KARIGARS if the loss in the course of melting and manufacturing of gold is beyond the specified agreed percentage then the value of such loss shall be adjusted from the payment due to KARIGARS. Accordingly in the present case more loss was incurred by the KARIGARS therefore the less or no payment was made and it is not the case that the gold was left with the KARIGARS in the form of payment. On the other hand, Ld. DR relied on the orders of authorities below.

10. From the aforesaid facts we find that in some cases less gold was received back from KARIGARS on account of loss of gold incurred during the course of melting and manufacturing process. Such a loss was treated by the

AO as payment to the KARIGARS in the form of gold without TDS. However the learned AR submitted this loss does not represent the payment to the KARIGARS in the form of gold but it is actual loss and the deduction for such access loss was also made from the payment of the KARIGARS. Now the question before us is whether such loss represents the payment to the KARIGARS or it is actual loss. In our considered view that there is undoubtedly loss occurred in the course of melting and manufacturing process of gold. These melting and manufacturing activities are carried out by the KARIGARS who are paid the service charges in the form of cash as per the market prevailing system. Accordingly we opined that the aforesaid loss cannot be termed as payment to KARIGARS. As per the order of the AO the assessee duly explained the loss of gold incurred during the course of melting and manufacturing process to the tune of 906.880 grams. Such a loss was not doubted by the AO at the time of assessment but the addition for the loss of gold 166.170 grams was made due to non-availability of reconciliation. In our view merely assessee failed to provide the reconciliation does not mean that the payment has been made in the form of gold. The AO should have brought cogent reasons for treating the loss of gold as payment to the KARIGARS. As we find that the loss of 906.880 grams was duly explained which shows that there was the system of making the payment in cash to the KARIGARS. Accordingly we held that the less gold received from the KARIGARS cannot be termed as payment to KARIGARS. Therefore we have no hesitation to reverse the orders of authorities below. Hence this ground of appeal of the assessee is allowed.

11. Third issue raised by assessee in this appeal is that the learned CIT(A) erred in confirming the order of AO by making addition of Rs.45,872/- on account of non-production of the reconciliation statement of the gold deposit lying with the assessee. For this, assessee has raised effective ground as under:-.

> *"3) That the Learned Commissioner of Income Tax (Appeals) erred in confirming the addition of Rs.45,872 made by the Assessing Officer on the alleged ground that the assessee could not reconcile and file evidences in respect of gold deposits lying with the assessee.*

12. The assessee has shown gold deposits from customers for 2173.07 grams. Some of the gold items were lying with the assessee for more than 3 years. At the time of assessment the assessee failed to reconcile the gold deposit for 30.100 grams. Accordingly the AO treated the value of such unexplained gold as income of the assessee. The value of such gold was worked out Rs.45872.00 (30.100 grams X Rs. 1524). The AO accordingly made the addition of Rs. 45872.00 to the total income of the assessee.

13. Aggrieved, assessee preferred an appeal to Ld CIT(A). The assessee before the ld. CIT(A) submitted that such gold deposit does not relate to the year under appeal and it has not been written off in the books of accounts. Therefore the provisions of section 41(1) of the Act will not be applied in the instant case. The learned CIT(A) disregarded the claim of the assessee and confirmed the action of AO by observing as under:-

> *"7. Appeal on ground no. 4 is against the addition of Rs.45872/- on account of gold deposits to customers. During the assessment proceedings while examining the closing stock the AO found gold deposit from customers of over 2 kg. the AO asked the assessee to reconcile the deposits and excess stock found. The AR submitted a reconciliation statement but could not either reconcile or explain gold of 30.100 grams. Thus, the AO applied rate of gold at Rs.1524 per gram and made an addition of Rs.45872/- for excess unexplained and un-reconciled gold found. During the appellate proceeding the AR could not explain or contradict the finding of the AO, therefore, assessee's appeal on ground no. 4 is dismissed."*

Being aggrieved by this order of Ld CIT(A) assessee is in second appeal before us.

14. We have heard rival contentions and perused the materials available on record. Before us ld. AR submitted that gold was deposited by the customers and the same has been reflected in the books of accounts and none of the liability with regard to the gold deposit has been written off in the books. Therefore the question of treating the unexplained gold as income does not arise. On the other hand the ld. DR relied on the order of authorities below.

15. From the aforesaid discussion, we find that the assessee at the time of assessment framed by the AO the assessee failed to reconcile the gold received from the customers to the tune of 30.100 grams therefore the same was treated as income. However from the submission of the assessee we find that the liability towards the deposit of gold from the customers was very much reflecting in the books of the assessee for the relevant year and no such liability was written back in the year. Now it is really clear that a trading liability can be taxed only if it is written off in the books of accounts. In the instant case although the assessee failed to give the reconciliation but such liability was not written off in the books of accounts. Accordingly in our considered view the aforesaid liability cannot be termed as income under section 41(1) of the Act. On contrary ld. DR failed to bring anything on record to controvert the argument of the assessee. So the liability towards the deposit of gold cannot be treated as income of the assessee. Hence ground of appeal of the assessee is allowed.

16. **In the result, assessee's appeal stands allowed.**

Order pronounced in the open court 13/04/2016

Sd/-	Sd/-
(N.V.Vasudevan)	(Waseem Ahmed)
(Judicial Member)	(Accountant Member)

Kolkata,

*Dkp
दिनांकः- 13/04/2016 **कोलकाता** ।

आदेश की प्रतिलिपि अग्रेषित / Copy of Order Forwarded to:-

1. अपीलार्थी/Appellant-Surovi Mansion Jewellers Pvt. Ltd., 195/13B, Rash Behari Avn.Kol-19
2. प्रत्यर्थी/Respondent-ITO Ward-12(1), 3 Govt. Place, Kolkata-700 001
3. संबंधित आयकर आयुक्त / Concerned CIT Kolkata
4. आयकर आयुक्त- अपील / CIT (A) Kolkata
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, **कोलकाता** / DR, ITAT, Kolkata
6. गार्ड फाइल / Guard file.

By order/आदेश से,

/True Copy/

उप/सहायक पंजीकार
आयकर अपीलीय अधिकरण,
कोलकाता ।