

**IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH: 'E', NEW DELHI**

**BEFORE SH. BHAVNESH SAINI, JUDICIAL MEMBER
AND
SH. O.P. KANT, ACCOUNTANT MEMBER**

ITA No. 6884/Del/2014
Assessment Year: 2010-11

Income Tax Officer, Ward - 24(4), New Delhi	Vs.	M/s. Neoteric Digital Embedded System, D-2/2482, Vasant Kunj, New Delhi
PAN : AAGFN8381F		
(Appellant)		(Respondent)

Appellant by	Sh. M. Barnwal, Sr.DR
Respondent by	Sh. Vidhur Puri, CA

Date of hearing	24.08.2017
Date of pronouncement	06.10.2017

ORDER

PER O.P. KANT, A.M.:

This appeal by the Revenue is directed against order dated 17/10/2014 passed by the Commissioner of Income-tax (Appeals)-XXIII, New Delhi [in short ~~the~~ CIT-(A)] for assessment year 2010-11, raising following grounds:

- 1. On the facts and in the circumstances of the case the Ld. CIT(A) has erred in deleting addition of Rs.86,59,086/- made by the AO without appreciating the facts of the case.*
- 2. On the facts and in the circumstances of the case the learned CIT(A) has erred in allowing the deduction u/s 80-IC because the enquiries conducted during the assessment proceedings suggested that the manufacturing unit of the assessee does not exist in the notified area as claimed by the assessee.*

3. *On the facts and in the circumstances of the case the learned CIT(A) has erred in allowing the deduction u/s 80-IC as the extremely poor consumption of electricity is a strong indicator of non-existence of business.*
4. *The appellant craves leaves to add, alter or amend any of the grounds of appeal before or during the course of hearing of the appeal.*

2. Briefly stated facts of the case are that the assessee filed return of income on 09/10/2010 declaring nil income. The case was selected for scrutiny and notice under section 143(2) of the Income Tax Act, 1961 (in short ~~the~~ Act) was issued and complied with. In the scrutiny proceedings, the Assessing Officer disallowed the claim of deduction under section 80IC of the Act amounting to Rs.86,59,086/-. The assessee claimed deduction under section 80IC of the Act for development of a software, which automatically controlled the inbuilt generators installed beneath telephone towers for communication. The learned CIT-(A) allowed the appeal of the assessee following the order of the Commissioner of Income-tax (Appeals)-I, Dehradun in the case of the assessee in immediately preceding assessment year i.e. 2009-10. Aggrieved, the Revenue is in appeal before the Tribunal raising the grounds as reproduced above.

3. In the grounds raised, the Revenue has contended that the manufacturing unit of the assessee was not in existence and, therefore, the Ld. CIT-(A) has wrongly allowed the deduction under section 80IC of the Act.

4. Before us, the Ld. Sr. DR relied on the order of the Assessing Officer and submitted that poor consumption of the electricity supported the finding of the Assessing Officer that manufacturing unit of the assessee was not in existence. Without prejudice to his arguments, the

Ld. Sr. DR further submitted that alleged activity of software development was not amounted to manufacturing and, therefore, also the assessee was not eligible for deduction under section 80IC of the Act.

5. On the other hand, the learned counsel of the assessee submitted that issue in dispute is covered by the order of the Tribunal in the case of the assessee for assessment year 2009-10. He submitted that in assessment year 2009-10, the Commissioner of Income-tax (Appeals)-I, Dehradun, examined documentary evidences including the certificates issued by the Central Excise Authorities regarding existence of the unit and the Tribunal upheld the finding of the Ld. Commissioner of Income-tax(Appeals)-I, Dehradun.

6. We have heard the rival submission and perused the relevant material on record. In assessment year 2009-10, the Assessing Officer disallowed the deduction under section 80IC of the Act on the ground that unit of the assessee claiming deduction was not found to be in existence. In assessment year 2009-10, the Tribunal in ITA No. 1300/Del/2013 allowed the deduction under section 80IC of the Act. The relevant extract of the order of the Tribunal is reproduced as under:

“5. We have heard the rival submissions and perused the material on record. The Assessing Officer held that the assessee failed to prove the existence of the unit at the given address as at the time of site inquiry, a unit dealing in rubber products was found at the premises. Before the learned Commissioner of Income-tax(Appeals), the assessee filed copy of rental agreement for the premises, documents in support of power connection, documents in relation to registration of the unit with the District Industry Centre, Roorkee, District Haridwar, documents of registration with the Central excise Department and visit by the Central Excise Authorities, registration under VAT and CST with commercial taxes Department of Government of Uttarakhand, no objection certificate from pollution-control authorities, in support of its contention that the unit was setup at said premises. The assessee submitted that the unit was closed w.e.f. 16/08/2010 due to rapidly diminishing demand

and resulting cancellation of the orders to its suppliers. The assessee further submitted that the unit of the assessee was closed down w.e.f. 16th of August 2010, whereas, the AO made the site visit at the time of assessment proceedings somewhere about the end of the year 2011, and therefore he doubted the existence of the unit at the said premises. The assessee also filed copy of the documents referred above in the paper book before us. Having gone through the documents, the finding of the AO that the unit was not in existence at the given address, is not sustainable.

6. Further, the AO observed that net profit of the assessee company was abnormally high and leads to channelize the income of the assessee from undisclosed sources. In respect of this observation of the Assessing Officer in the assessment order, the assessee before the learned Commissioner of Income-tax(Appeals) submitted that product of the assessee were having software embedded in the hardware and the software enhanced the value of the product. The assessee further submitted that cost of the hardware was very less whereas the software was developed in-house as the partners were having expertise in specialized field of embedded software systems and because of that, they were able to command a high profit margin on their products and therefore cannot treat the same as income from undisclosed sources. Further, the assessee also submitted that most of the transactions of purchase and sales were through cheque and there were only negligible cash transaction. The learned Commissioner of Income-tax(Appeals) held that the allegation of high net profit rate, unless substantiated by any finding showing that the same was not genuine, cannot be the basis for disallowing the assessee's book result. Before us, also the Ld. Senior DR could not bring any material that undisclosed income was rooted in the books of the assessee and any comparable cases which could establish that the gross profit rate was abnormal in the line of assessee's business. The learned Commissioner of Income-tax (Appeals) has also dealt the objection of the Assessing Officer of having plant and machinery only of Rs. 60,985/- and it was not possible to have manufacturing of goods worth crores of rupees, no expenses on freight inward or outward, no quantitative details of principal items such as raw material, finished goods, byproducts etc in the tax audit report. The relevant findings of the learned Commissioner of Income-tax(Appeals) are reproduced as under:

“1.5.1 According to the AO, the assessee had shown turnover of Rs.3 crore but had plant machinery of only Rs.60,985/ in the balance-sheet. In this connection, the assessee has made the following submission:

“We wish to inform your goodself that manufacturing of embedded systems requires mounting of components on a printed circuit board. Boards and components are purchased from external parties. The micro- controller, which, is the heart of the system, are also purchased from external parties and programmed. Once all items are available, a technician will mount the components on the PCB and solder them. A typical soldering station will require less than 100 Watts of power. The system is powered on using a 12V battery and the consumption of current in the system is in milli-amperes. The micro controller performs a self- test and checks all components are healthy and working. Once the test is passed, the system is ready. Given the huge dependence of the system on software and its capability to perform self-diagnostics and test, there is really no need for any huge plant and machinery. The operating voltage and operating current are also so less that the power consumption is indeed very less. Also there is no dependence of the manufacturing process on 'temperature, humidity etc or other environmental factors.

It has been already informed to the assessing officer that the partners of the assessee firms are qualified engineers as Mr. S.P. Tiwari is an Electrical Engineer from the prestigious Benaras Hindu University, Varanasi, UP and Mr. Saurabh Tiwari is a software Engineer from Institute of Engineering and Technology, Lucknow, UP.

Mr. S.P. Tiwari has served the Indian Air Force as Aeronautical Electronics Engineer for 30 years. He had a splendid career in the Indian Air Force, and retired as a very senior officer (Air Commodore) in 1999. His work required him to design, develop, maintain & repair electronic systems for missiles, radar and communication used in advanced fighter jets of the Indian Air Force. For his expertise and outstanding contribution he has been awarded the Vishesh Sewa Medal from the President of India.

Mr. Saurabh Tiwari is a software engineer who has worked for more than 5 years in one of the biggest software companies of the world(Adobe Systems Inc.) which is head quartered in USA. During his career at Adobe Systems, he received an Outstanding Contribution Award for his work in design and development of software for Adobe' market leading product called Adobe Acrobat. Also, during his tenure, he invented a software technology to identify Logical Elements in a PDF document. This invention has been patented by Adobe Systems in the United States Patent Office, and is considered to be an original invention.

In light of the above facts, it can be properly seen that the owners of NDES are persons of who have received not only national but also

international recognition for their work in the areas of design and development of software and electronic embedded systems. Such a team is more than capable of designing and developing the products which were manufactured by the assessee firm.

Now, it is very clear that the partners of the assessee firm are self sufficient and do not require to pay any royalty to anyone."

1.5.2 The business was primarily of software-development; the hardware part was of secondary importance. It did not require heavy investment in plant and machinery. The partners are technically qualified persons who were doing the software part themselves. The low investment in plant and machinery was a ground for raising doubt about the assessee's business results. But, if heavy investment in plant and machinery was not actually required for the business process, it stands to reason that the same was not made by the assessee.

1.6.1 According to the AO, the assessee had not debited expenses on freight inward or outward. In this connection, the assessee has made the following submission:

"That the assessee was not in the manufacturing of any big items which requires heavy freight & cartage inward or outward. The assessee unit was in the business of manufacturing of embedded software systems which are small, low power systems which run on battery. They require little freight & cartage which was borne by the seller at the time of purchase or raw material & by the purchaser at the time of sale of finished goods.

All inward material has been accompanied with Form-16 that is checked on the border of Uttarakhand and stamped. The assessee has received Form-C and Form-11 from customers who have bought the material manufactured by the assessee."

1.6.2 Conventional thinking suggests that, if manufacturing takes place, there should be freight expenses, both inward and outward and, if they are not there, the genuineness of the business results may be doubted. But, the assessee has furnished proper explanation. Its submission that the freight was borne by the supplier/s on the input and by the customer/s on the output may appear unusual but" is not improbable. If the AO doubted the contention, he was free to conduct enquiry with the suppliers as well as customers. If he did not do so, he cannot reject the contention on the basis of suspicion. On the other hand, the assessee has claimed that the movement of goods inwards was duly documented by way of sales tax Form-16 (subjected to verification at the Commercial tax check post at the entry point in Uttarakhand) and the movement outward was by Form-C and Form-11 from customers. Hence, no adverse inference can be drawn from this.

1.7.1 According to the AO, quantitative details of principal items such as raw material, finished goods, bye-products, etc. were not furnished in the tax

audit report. In this connection, the assessee has made the following submission:

"We wish to bring to your kind knowledge that there is no by-product in the manufacturing of embedded software systems. As such our product was not a general purpose retail product. Our production schedule was based on extract demand raised by our customer who used to supply to BSNL. It has been clearly mentioned in Form No. 3CD, by the Auditor of the assessee that due to the nature of the business, it is not possible to give quantitative details.

The assessee has maintained proper books of accounts, bills & vouchers & all the sales & purchase have been properly submitted to the VAT Deptt. on quarterly basis which have been acknowledged by VAT Deptt."

1.7.2 The explanation is self-explanatory. Even if the assessee did not furnish quantitative details, its books of account were available for verification. Unless some discrepancy was pointed out in the same, the non-furnishing of quantitative details in the tax audit report, by itself, would not mean much.

1.8 The assessee furnished copies of the following documents in support of its contention:

- 1. Partnership Deed dt. 01.06.2008.*
- 2. Qualification/achievement certificates of the Partners.*
- 3. Rent deed.*
- 4. DIC Registration (Part-1).*
- 5. Vat Inspection Report.*
- 6. Vat Registration Certificate.*
- 7. NOG from Pollution Office.*
- 8. Electricity Certificate.*
- 9. Declaration to Central Excise.*
- 10. Excise Inspection Report.*
- 11. Sample of Purchase Bills alongwith FORM 16.*
- 12. Sample of Sale Invoices.*
- 13. Rent Deed for Tyre Manufacturing plant which was causing pollution.*
- 14. DIC Registration Part-2).*
- 15. Letter to Excise for closure.*
- 16. Closure acknowledgement from Vat Department.*
- 17. Closure Information to DIC.*
- 18. Final Meter Sealing Certificate.*
- 19. Sales Tax Assessment Certificates.*

1.9 The foregoing analysis shows that the AO noticed some unusual features in the assessee's business and became suspicious of its genuineness as well as profitability. That was alright. But, he did not find any positive discrepancy in the assessee's books of account and other documents relating to the business that were produced before him. Nor did

he get adverse evidence on the basis of his independent enquiry. On the other hand, the assessee has furnished adequate explanation for all these unusual features of its business. The partners of the assessee firm are highly qualified technocrats. The father is a Vishishta Seva Medal (VSM) decorated retired officer of the Indian Air force and was noted for his expertise in communication electronics. The son is a distinguished computer scientist who had won accolades while working with Adobe Inc. They got together to do business for BSNL, supplying their product through the main vendor Vrinda Nano Technology (VNT). Initially, they did good business. But, soon the business environment deteriorated and they decided to stop the operations in Uttarakhand. The closure of the business was duly carried out, under intimation to all the authorities concerned. Considering the facts and circumstances of the case, the explanation furnished by the assessee and documents submitted by it, the inference drawn by the AO is not sustainable. He is directed to allow deduction u/s 80-IC to the assessee.

7. From the above, we find that the learned Commissioner of Income-tax (Appeals) after considering the submission of the assessee and in view of the available evidences, held that the inference drawn by the Assessing Officer was not sustainable. We are also agreed with the findings of the learned Commissioner of Income-tax(Appeals), as in the light of evidences produced by the assessee on the issue in dispute, no contrary decision can be arrived at. The finding of the learned Commissioner of Income-tax(Appeals) are, thus, well reasoned and we do not find any infirmity in the same. Accordingly, we uphold the finding of the learned Commissioner of Income-tax (Appeals). The ground of appeal of the Revenue is dismissed.”

7. We observe that in immediately preceding assessment year, the assessee has filed sufficient evidence of existence of unit at the address i.e. village Salempur, Rajputana, Roorkee, district Hardwar (Uttaranchal), and accordingly the Tribunal accepted the finding of the Ld. Commissioner of Income-tax(Appeals) . I, Dehradun for holding that the unit was in existence during relevant period .

8. Since in the year under consideration, the identical issue of denying deduction under section 80IC of the Act on the allegation of non-existence of the unit is involved, respectfully following the decision of the Tribunal (supra), we uphold the finding of the Ld. CIT-(A) on the issue in dispute and dismiss the grounds of the appeal.

9. We may like to specifically mention that in the grounds of appeal the Revenue has not raised any ground challenging whether the software development activity of the assessee was not manufacturing and, therefore the arguments of the Ld. Sr. DR challenging the deduction under section 80IC of the Act in this regard, cannot be considered.

10. In the result, the appeal of the Revenue is dismissed
The decision is pronounced in the open court on 6th Oct., 2017.

Sd/-
(BHAVNESH SAINI)
JUDICIAL MEMBER

Dated: 6th October, 2017.
RK/(D.T.D)

Sd/-
(O.P. KANT)
ACCOUNTANT MEMBER

Copy forwarded to:

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

Asst. Registrar, ITAT, New Delhi