IN THE INCOME TAX APPELLATE TRIBUNAL SURAT BENCH, SURAT

BEFORE SHRI AMARJIT SINGH, JM & SHRI O.P.MEENA, AM

ITA No.202/Ahd/2012

(**Assessment Year 2008-09**)

Dy. Commissioner of Income Tax, Circle-3, Surat		M/s. Jariwala Enterprises, 120-121, Abhikram, Opp. Bhulka Bhavan School, Adajan, Surat-395010.
PAN/GIR No.AACFJ0019L		
Appellant)	..	**Respondent**)

Revenue by	Shri B. P. K. Panda (Sr. DR)
Assessee by	Shri Mehul R. Shah
Date of Hearing	**25/09/2019**
Date of Pronouncement	**30/09/2019**

O R D E R

***PER AMARJIT SINGH (J.M)*:**

The revenue has filed the present appeal against the order dated 13.10.2011 passed by the Commissioner of Income Tax (Appeals) – Majura Gate, Surat [hereinafter referred to as the "CIT(A)"] relevant to the A.Y.2008-09.

2. The revenue has raised the following grounds: -

1 *On the facts and circumstances of the case and in law, the Ld. CIT(A)-II Surat has erred in deleting the addition of Rs.2,46,96,370/- made on disallowance of total expenses of sales promotion and rate different without appreciating fact that the assessee has violated provision of Accounting Standard-I relating to disclosure of accounting policy u/s 145(2) and also invoking of provision of u/s 145(3) of the I.T. Act.*

2. *On the facts and in the circumstances of the case, the Ld. CIT(a) ought to have upheld the order of the AO.*

3. *It is therefore, prayed that the order of the CIT(A) may be set-aside and that of AO may be restored to the above extent.*"

3. The brief facts of the case are that the assessee filed its return of income on 29.09.2008 declaring total income to the tune of Rs.95,10,370/- for the A.Y. 2008-09. The case was selected for scrutiny. Notices u/s 143(2) & 142(1) of the Act were issued and served upon the assessee. As per the tax audited report u/s 44AB, the nature of business of assessee was stated to be the dealer in commercial goods, electric goods, mobile etc. as an agent of Nokia and dealer in

DVD players, home-theatre, etc., of Phillips. According to the para-11(a), the assessee was following mercantile system of accounting and there was no change during the year in the method of accounting employed viz. method employed in the immediately preceding year. On appraisal of the para 28(a) of the tax audit report, it came into noticed that the quantitative detail of principle items of goods traded were not given:- (i) Opening Stock (ii) Purchases during the year (iii) Sales during the year (iv) Closing stock (v) Shortage of stock excess, if any. On appraisal of the P & L Account, it was noticed that the assessee has credited the following indirect income:- (i) Rate difference at Rs.4,52,14,653/- (ii) Sales Promotion/reimbursement at Rs.98,83,507/- (iii) Commission at Rs.10,62,240/-. The notice u/s 133(6) was issued to M/s. HCL Infinite Ltd. and Nokia India (P) Ltd. calling for following information. Both the companies furnished the information, the assessee failed to justify the claim of expenses of Sale Promotion and Rate difference on the subject mentioned in the assessment year in sum of Rs.2,46,96,370/-, therefore, the said amount was added to the income of the assessee and the total income of the assessee was assessed to the tune of Rs.3,42,06,740/-. Feeling aggrieved, the assessee filed an appeal before the CIT(A) who allowed the claim of the, therefore, the revenue has filed the present appeal before us.

4. We have heard the arguments advanced by the Ld. CIT(A) Representative of the parties and perused the record. The Ld. Representative of the assessee has objected the additional grounds raised by revenue on the basis of this fact that the additional ground has been taken very late, therefore, the additional grounds is not liable to be taken into consideration in accordance with law. However, on the other hand, the Ld. Representative of the Department has refuted the said contention. At the time of filing the appeal, the revenue has challenged the deletion of the addition of Rs.2,46,96,370/-. Thereafter, the additional ground were taken which bifurcated the amount of Rs.2,46,96,370/- belonging to the different head. In fact, the basic ground has been bifurcated in accordance with the disallowance of different head but the amount is the same. Therefore, we

nowhere found any illegality on account of raising the additional ground subsequently because the additional ground is the part and parcel of the basic ground in which the deletion of addition in sum of Rs.2,46,96,370/- has been challenged. Accordingly, we admit the additional ground.

ISSUE No. 1 to 5

5. Issue nos. 1 to 2 are related to the deletion of addition on account of Rs.2,46,96,370/-. In ground no. 3, the revenue has challenged the deletion of addition which is the part of the said amount of Rs.1,50,41,236/- and 96,55,134/-. The Ld. Representative of the revenue has argued that an amount of Rs.1,50,41,236/- was not accounted in the P & L account, therefore, the same was not genuine but the CIT(A) has wrongly allowed the same. It is also argued that in sum of Rs.96,55,134/- which was not accounted in the earlies years has also been allowed wrongly and illegally, therefore, the finding of the CIT(A) is not justifiable. Before going further, we deem it necessary to advert the finding of the CIT(A) on record.:-

> *"8. I have gone through the facts of the case, assessment order, submissions of the assessee, evidence filed, remand report and the comments of the appellant in response to the remand report. The books of accounts were primarily rejected as the AO was of the opinion that the accounting standard-I had not been followed as net amount of indirect income had been mentioned in the P&L account as against gross receipts and this fact was not disclosed in the notes accompanying the accounts. He concluded that the statement of account of the assessee did not disclose true & fair view of business transactions. He therefore considered the amount of Rs.24696370/- as income of the appellant or in other words did not admit the claim of the assessee regarding amounts passed on to retailers. The question to be decided is whether mentioning "net" indirect income and not "gross" indirect income for the purpose of profit & loss account is sufficient to reject books of accounts citing violation of AS-1. It is also to be decided whether all payments/deductions made out of gross receipts can be considered as income of the assessee simply because net figure of income had been reported in the profit & loss account irrespective of the fact that such payments/deductions were duly recorded in the books. Accounting Standards has been made mandatory since 01.04.1997. The assessee has been following the same accounting procedures/systems in earlier years and these have been accepted accounting policies had not been properly disclosed. In the remand report the A.O. is all but silent as to*

the violation except stating that quantitative details were also not mentioned in the tax audit reports. The assessee has accounted for the receipts in the year of accrual and this was explained to the A.O. by production of relevant ledger accounts and financial statements of respective accounting periods. The A.O. has not shown that these receipts have not been accounted for in preceding years. Similarly payments to retailers have been mentioned in the books. The quatitative details were provided to the A.O. during assessment proceedings and reconciled with the details obtained by the A.O. from HCL/NOKIA. The reconciliation has been accepted by the A.O. The P&L account is but a reflection of the books of accounts. It is the books of account which are required to be rejected but the books properly record the business transactions. The purpose of Section 145 including prescribing Accounting Standards is to determine the income of the assessee which even after rejection of books has to be done in a judicious manner. It cannot be arbitray. In this case recording Net income instead of Gross receipts have no, effect on the profits of the assessee. Even if it is considered that AS-1 has not been followed and accounts are rejected, then also additions of the kind made by the A.O. cannot be made as such income has been duly credited in the I books, albeit for a preceeding year on accrual basis and expenses disallowed have been recorded in the books. Additions could be made only if it could be shown that the expenses were not genuine or incomes had not been recorded. This is not the case here as the A.O. has made the addition only because accounts were rejected. Neither such a rejection nor such an addition can be sustained only on the technical premise that AS-1 has not been followed. Even otherwise, the assessee has disclosed in its financial statements that it was following mercantile system of accounting; the accounting system & procedure was regularly followed by it; the accounting system and procedure followed by it had been accepted by the Department; all relevant details regarding the indirect income were provided to the A.O. and wherever required the figures were reconciled; and these reconciliation were not shown to be incorrect. Therefore, in my opinion, there was no reason for rejection of books and making the addition in respect of income already recorded in earlier years and amounts paid to retailers on this basis.

8.1 Though rejection of books by the A.O. has not been upheld, the same amounts have been disallowed on different grounds and these have also been agitated by the appellant. In concise grounds of appeal No. 2 the assessee has claimed that the amount of Rs 9655134/- should not have been disallowed as this has already been accounted in earlier years on mercantile basis when it j raised claim on the HCL/NOKIA. The A.O. has disallowed the amounts in' para-12 of the assessment order by holding that the amount is to be accounted on receipt of credit notes from HCL/NOKIA which were not received and therefore, it should be inferred that amounts have not been accounted by the assessee. The said addition has been made by the

A.O. on wrong understanding of mercantile system of accounting. In mercantile system, the income has to be accounted at the time of accrual or receipts, whichever is earlier. The appellant raised demand on HCL/NOKIA and on raising of such demand the income accrued to him and he was therefore required to record the income in the same year. The assessee has accordingly shown these amounts in the relevant years irrespective of receipts which were in the current year. All details alongwith relevant evidences regarding accounting of these receipts in preceding years were placed before the A.O. during the assessment proceedings. The A.O. has not shown that the income has not been accounted in the preceding year. Once the income has been accounted for in a preceding year on accrual basis, it cannot be added on receipt basis in subsequent year as it would amount to taxing the same income twice. The addition of Rs.96,55,134/- vide para-12 of the assessment order is without any basis and deleted.

8.2. The A.O. also disallowed the reimbursement of Rs. 15041236/- made to retailers for sales promotion and price drops on the ground that these were not genuine. This conclusion was based on the report of the Inspector dated 28.12.2010. The Inspector had tried to verify 25 parties on the basis of address given on the vouchers of payment of retailers but could not locate any of the parties. The Inspector could also not locate Shri Chandresh Himatbhai Raja to whom motor cycle had been given as prize during A.Y. 2005-06. No identifications like PAN, TAN, sales-tax or VAT No. were mentioned on the vouchers of payment. The A.O. on the basis of such verification and lack of identification on vouchers considered the whole of expenses as not genuine. It was argued by the appellant that whole exercise had been carried out behind his back and the report was also not made available to him or any show cause issued. The appellant provided the name & address, shop establishment license, ledger account and confirmations from the persons who were test checked by the Inspector. It was also submitted that the credit notes issued to the retailers were produced before the A.O. who had verified it. On the basis of this information the Inspector carried out inquiries once again during remand and it is seen that all but six persons including Shri Chandresh Himatbhai Raja could be traced. In their comments to the remand report, it was submitted by the appellant that the six persons who could not be traced out may have closed their business in the three years since the accounting period. It was also submitted that the confirmations of these persons were on record. It was also pointed out that the total number of retailers serviced by the appellant were close to 1800 out of which only 25 had been subjected to verification and only six were not traceable even after three years and it was pleaded that no adverse inference

should be drawn from this. It was further submitted that the total amount of incentive paid to the six retailers not traceable was only Rs.63275/- which was negligible compared to the total quantum of expenses. As the details were before the A.O., the modus operandi of receipt and disbursal and its accounting were explained with evidence, the persons not traceable during assessment were largely traceable in remand and the fact that large number of retailers were serviced whereas verifications were carried out in few cases only, there really remains no ground for holding that the payment was not genuine. However, having said that it is also a fact that all the persons could not be traced and though there has been passage of time and credit note with signatures of the recipients is on record, in my opinion, retaining an addition of Rs. 1,00,000/- to cover for any discrepancy would be in the fitness of things. The addition is retained to this extent. This ***ground*** *is* ***partly allowed.***

8.3. The A.O. also disallowed the payments of Rs.24696370/- made to the retailers on the ground that these payments were in the nature of commission/incentive paid to agents without TDS. The A.O. after analysis of the agreement between HCL and the assessee held that the relation between the two was of principal and agent and the payments of sales incentive/promotions/price drops were in the nature of turnover commission. On the basis of this inference he further held that the relation between the assessee and his customers (retailers) which was because of the existence of the agreement between the assessee and HCL was similar in nature - i.e. principal and agent and that the character of payments being similar these were also commission/brokerage. He therefore concluded that the payments by the assessee (principal) to the retailers (agent) being commission /brokerage paid for achieving sales targets was hit by the provisions of section 40(a)(ia) as no tax had been deducted at source as required u/s. 194H.

It is seen that there was no agreement between the assessee and his customers, i.e. retailers. The disallowance of payments by the assessee to its customers is based on drawing parallel between its relation to its customers with relation of the assessee to HCL. While such an assumption itself may be questionable, even the inference regarding relation between the assessee and HCL is not based on correct reading of the agreement between them. I find that in coming to this conclusion, the A.O. has considered what was not in the agreement between HCL and the assessee. He has also not considered any of the evidence which was before him. Even from the excerpts of the agreement reproduced by the A.O. it is clear that the said clauses talk about "purchases" and not stock transfer to agent. The heading is "minimum purchase requirement"; 7.1 talks about prices to be paid by the assesseee to HCL; 7.2 talks about price changes; 7.4 talks about sales-tax, VAT, insurance, freight and any applicable

reporting to be the responsibility of the assessee; 7.5 states that stocks remaining unsold or obsolete would not be taken back i.e. it would be the assessee's responsibility; 8.1 states that "full payment in advance for purchases of the product" will be given to HCL; 8.2 states that interest would be charged for late payment. Only because there is no clause in the agreement for reimbursement of sales promotion expenses or payment on account of rate difference, the payments received on this account do not become turnover commission. Similarly, the nomenclature of "distributor" used in the agreement or the product sold remaining under the "warranty" of NOKIA will, and to the exclusion of all other clauses and evidences, alone define the nature of relationship between HCL/NOKIA and the assessee. Warranty, it may be mentioned always remains of the manufacturer and not the trader. The appellant had produced the invoices of sales raised by HCL/Nokia on them for sales of product. It also produced the invoices of sales raised by it on its customers. The ownership in goods. The appellant enjoyed CC limit from the bank on hypothecation of stocks. It has charged VAT on sales to its customers. The customers are shown as debtors in the books of the assessee. Hence, from the terms of the agreement as well as actual running of business, it is clear that the relation between HCL/Nokia and the assessee and between assessee and its customers is on principal to principal basis. Therefore, section 194H which is applicable in the case of principal and agent is not attracted in respect of payments made by assessee to its customers. The addition made for violation of Section 40(a)(ia) is deleted."

6. On appraisal of the above mentioned finding, we noticed that the CIT(A) has observed that no opportunity of being heard was given to the assessee before rejecting the books of account. It also came into noticed that the books of account were not examined by the AO. The books of account was rejected on the basis of this fact that quantative details were not mentioned in the tax audit report. The genuineness and in genuineness of claim were not examined by A.O. Each and every details had been mentioned in the P&L account and books of account. How the details were wrong, has not been mentioned by the AO in his order. The CIT(A) has discussed each and every aspects of the case. The remand report was also considered by CIT(A) also. The assessee claimed an amount of Rs.96,55,134/- which was accounted in earlier year on mercantile basis when it raised the claim on the HCL/Nokia. The AO has disallowed the amounts was to be accounted on receipt of credit notes from HCL/Nokia which were not received and therefore, it should be inferred that amounts have not been accounted by the

assessee. In fact, the appellant raised the demand on the basis of accrual in the same year and recorded accordingly. The assessee also showed the amount in the relevant years. The income was not shown in the preceding year. Once the income was accounted for in a preceding year on accrual basis, it cannot be added on receipt basis in subsequent year as it would amount to taxing the same income twice, therefore, the addition in sum of Rs.96,55,134/- was deleted. Nothing wrong was found in deletion the said addition. Now coming to the reimbursement of Rs.1,50,41,236/- made to retailer for sales promotion and price drops. The claim of the Assessee was rejected on this fact that the Inspector failed to verify the 25 parties. The appellant provided the name and address, shop establishment license, ledger account and confirmations from the persons who were test checked by the Inspector. The credit notes issues to the retailer were produced before the AO to verify it. At the time of remand report except 6 parties,all were tested and transactions were verified. Only in connection with 6 retailer, the amount involved in sum of Rs.63,275/- were not traceable. Therefore, taking into account of the records, when the claim of the assessee allowed in sum of Rs.1,00,000/- to cover for any discrepancy it seems that after proper verification the claim has rightly allowed. The other deletion of the disallowance is in connection with the provisions of Section 40(a)(ia) on account of this fact that the assessee failed to deduct the tax at source in view of the provisions u/s 194H. The provisions u/s 194H is applicable to the case of principal and agent whereas the same is not applicable to the payments made by assessee to its customers, therefore, the provisions u/s 40(a)(ia) was not applicable, hence, the CIT(A) has rightly deleted the addition. So far as the deletion of the disallowance of the provisions of Rs.28,18,234/- made on account of outstanding sales promotion expenses. We nowhere found illegality and infirmity in view of the finding of the CIT(A) which has been discussed above. There is no need to repeat the finding of the CIT(A). We nowhere found any fault or illegality to which it can be assumed that the finding of the CIT(A) is not justifiable. Taking into account all the facts and circumstances, we are of the view that the CIT(A) has decided the matter of

controversy judiciously and correctly which is not liable to be interfere with at this appellate stage. Accordingly, we decide these issues in favour of the assessee against the revenue.

7. In the result, the appeal filed by the revenue **is hereby ordered to be dismissed**.

Order pronounced in the open court on this 30/09/2019

Sd/- Sd/-

(O. P. MEENA) **(AMARJIT SINGH)**
ACCOUNTANT MEMBER **JUDICIAL MEMBER**

सुरत/ **Surat, Dated:** 30/09/2019/Vijay Pal Singh, *Sr.PS*
Copy of order sent to- Assessee/AO/Pr. CIT/ CIT (A)/ ITAT (DR)/Guard file of ITAT.

By order

Assistant Registrar, Surat