

IN THE INCOME TAX APPELLATE TRIBUNAL DELHI

(DELHI BENCH 'B' : NEW DELHI)

BEFORE SH. N.K.BILLAIYA, ACCOUNTANT MEMBER

AND

SH. ANUBHAV SHARMA, JUDICIAL MEMBER

ITA No. 8709/Del/2019

(Assessment Year : 2015-16)

ACIT, Circle-63(1), New Delhi	Vs.	Friends Medicos Shop No. 6, MCD Shopping Complex, Asaf Ali Road, New Delhi-110055 PAN : AAFF9675Q
(APPELLANT)		(RESPONDENT)

Appellant by	Sh. Ved Jain, Adv.
Revenue by	Sh. Vivek Kumar Upadhyay, Sr. DR

Date of hearing:	17.07.2023
Date of Pronouncement:	10.10.2023

ORDER

PER ANUBHAV SHARMA, JM:

The appeal has been preferred by the Revenue against the order dated 02.08.2019 of CIT (A)-38, New Delhi (hereinafter referred as Ld. First Appellate Authority or in short Ld. 'FAA') arising out of an appeal before it against the order dated 30.12.2017 passed u/s 143(3) of the Income Tax Act, 1961 (hereinafter referred as 'the Act') by the ACIT, Circle-63(1), New Delhi (hereinafter referred as the Ld. AO).

2. Heard the Ld. Representatives of the parties and perused the record.

3. This is an appeal filed by the Revenue against the order of CIT(A) deleting additions of Rs. 2,05,29,361/- made by AO by estimating Net Profit before remuneration at 5.206% on account of rejection of books of accounts of the assessee u/s 145(3). The assessee is a partnership firm engaged in the business of trading of drugs and medicines and allied products including its distribution and also act as a stockiest for allopathic medicines. The assessee has filed its return of income on 24.09.2015 declaring total income of Rs 3,47,26,760/-. During the year under consideration, a survey u/s 133A was carried out in the premises of the assessee on 14.10.2014 wherein certain discrepancies were observed in the stock and cash balance which was voluntarily surrendered and offered for taxation. Thereafter the case of the assessee was selected for scrutiny and notice u/s 143(2) dated 28.09.2016 was issued to the assessee.

3.1 The AO vide notice dated 22.12.2017 alleged that the assessee has lowered his profits by manipulating its books of accounts by deflating partners' remuneration and inflating other expenses to artificially compensate for the income surrendered by the assessee on account of survey done in the month of October 2014. The AO also alleged that the net profit figure reported by the assessee is tainted and asked the assessee to show cause why the books of accounts be not rejected u/s 145(3) of the Act.

3.2 In response to the notice the assessee filed replies dated 21.12.2017 & 27.12.2017 (PB Pg. 377-379 & 385-391) explaining in detail the reason for fall in Gross profit, fluctuations in expenses and consequently decline in Net

Profit. The assessee submitted that net profit before remuneration has declined by Rs.2,09,67,550/- which was due to the following factors:

S. No.	Particulars	Amount (Rs.)
1	Gross Profit Declined (4,12,72,944-3,66,42,122)	46,30,822
2.	Other Income consist of commission and other declined (1,90,00,779 + 488,336-1,1,3,75,512-1,780-2,53,427)	78,58,416
3.	Bank charges and Interest (35,38,633-14,85,905)	20,52,728
4.	Charity & Donation (6,02,850-76,052)	5,26,798/-
5.	Bad Debts (17,10,450-4,24,897)	12,85,553/-
6.	Interest to Partners (1,14,99,711-87,94,159)	27,05,552/-
	Total	1,90,59,869

3.3 It was also submitted before the AO that –

Decline in GP was due to the fact of discontinuation of Institutional sales of Delhi Office mainly to B L Kapoor Memorial Hospital & Max Healthcare Institute Ltd to whom sales of Rs 5,99,754/- had been made against total sales of Rs.5,94,63,792/- in the proceeding financial year. Thereafter, the assessee sold its products at low margin to coup up in the industry.

Decline in commission income and other receipts - During the year under consideration, assessee had earned commission income from two parties,

namely-M/s Baxter (India) Pvt. Ltd. and M/s Roche Products India Pvt. Ltd. However, business with Baxter (India) Pvt. Ltd had substantially reduced from Rs.1.16,74,572/- in FY 2013-14 to Rs.11,78,280/- in FY 2014-15 i.e. present year. A copy of ledger A/c of Baxter (India) Pvt. Ltd. is also placed at PB Pg. 114 in which two entries of commission dated 14.04.2014 amounting to Rs.72,810 (Rs.64,880 + S.Tax Rs.8,010) & dated 01.01.2015 amounting to Rs 12,51,106 (Rs.11,13,480 + S.Tax 1,37,626) are recorded TDS had also been deducted on such income the same is also reflected in Form 26AS placed at PB Pg. 107 wherein it can be clearly seen that total amount paid/credited by Baxter (India) Pvt Ltd. is Rs.11,78,282/-.

Increase in Bank Charges and Interest-because of paucity of funds and poor recovery from customers. Also the assessee has no control over such expense and the assessee can in no way manipulate it. The assessee also submitted a copy of ledger A/c of Bank Interest and Bank Interest Certificate which are placed at PB Pg. 231 and PB Pg. 232-233 respectively.

Increase in Charity & Donation- The assessee has submitted complete details of donations made during the year which are placed at PB Pg.214. These donations have been made via banking channels as is evident from the ledger A/c of Charity & Donation Expenses placed at PB Pg.215. Relevant donation receipts have also been submitted by the assessee which are placed at PB Pg. 217-219. However, these expenses have been voluntarily added while computing taxable income as is evident from computation of income placed at PB Pg.2.

Increase in Bad Debts -due to recoverability of funds. The assessee had also filed a suit against those parties but could not recover any amount since those

parties absconded. Therefore, the assessee had written off those amounts as bad debts in the books of accounts.

Increase in Interest to Partners - Paid/credited in accordance with partnership deed.

Apart from the increase in abovementioned expenses, various other expenses had increased/decreased normally whose net adverse impact on the profitability comes to Rs.20,79,194/-. The assessee also submitted a comparative chart of expenses incurred for FY 2013-14 & FY 2014-15 which is placed at PB pg. 391.

4. However AO rejected the books of accounts and made addition of Rs. 2,05,29,361/- by computing the differential between average NP rate of 3 years before remuneration to partners vis-à-vis the NP declared by assessee. The assessee went in appeal where assessee had made rebuttal of the case of AO by submissions of which the important submission were as follows;

5. **Observation of AO;** The sales made to Max Healthcare as reported by the assessee of Rs. 5.99 lakhs was not in conformance with the response received from Max Healthcare Ltd. u/s 133(6) which reflected purchases of Rs. 9.16 lakhs from the assessee.

5.1 **Response of assessee;** The assessee transacts with Max Group which has two branches i.e. Max Healthcare Institute Ltd and Max Super Specialty Hospital. During the assessment proceedings, assessee had mentioned the sales of Max Healthcare Institute Ltd only amounting to Rs.5,99,754- (excluding sale tax amount) as is evident from PB Pg. 386 which after VAT comes to Rs.6,24,402/-. However, the assessee was not confronted with the response received from Max Healthcare u/s 133(6) during the course of

assessment proceedings. In such response received from Max Healthcare Institute Ltd. (Assessment Order Pg 21), AO has overlooked the fact that there were sales return of Rs.1,59,000/- as well and accordingly total sales made to Max Healthcare Institute Ltd was Rs.7,57,902/- instead of Rs. 9,16,902/-. Also, the assessee had recorded sales made to Max Super Specialty Hospital i.e. the other branch of Max Group amounting to Rs 1,33,500/-. Ledger A/cs of both Max Healthcare Institute Ltd and Max Super Specialty Hospital had also been submitted as additional evidence which are placed at PB Pg. 399. Therefore total sales to MAX Group comes to Rs 7,57,902 as per assessee's books which completely tallied with the balance reported by Max Group at Page 21 of the Assessment Order. Therefore, there is no difference in the transaction entered into by the assessee with Max Group and rejection of books on this ground does not hold good. In the remand report, though AO has accepted the sales return of Rs.1,59,000 but has not accepted the sales of Rs.1,33,500 made by assessee to Max Super Specialty Hospital claiming that during scrutiny no bifurcation of the accounts i.e, the Max Healthcare and Max Super Specialty Hospital appeared before AO. A copy of remand report dated 22.04.2019 is placed at PB Pg. 452.

6. **Observation of AO;** The GP rate should have risen on account of lesser sale transactions with Max healthcare which was yielding lower GP (5.19%) than the overall GP (FY 2013-14: 6.38%).

6.1 **Response of assessee;** The AO has failed to notice that it is the sales of institutional buyer which had reduced, In order to compensate such reduction in sales the assessee sold its products to customers, Sale of products to customers did not yield a gross profit margin equal to the margin from institutional buyers and thus it had resulted in overall decline in GP Margin.

Therefore, AO had misinterpreted the facts by holding that GP Rate should have rather increased on account of discontinuance of sale to Max Healthcare. Moreover, the GP Rate had consistently been falling over the preceding years.

7. Ld. CIT(A) considered the detailed submissions and justification provided by the assessee and has categorically held that the rejection of Books of Accounts was not justified. Relevant finding as appearing at Pg. 10 of the CIT(A) order is reproduced below:

"Every year is a different year owing to its facts and circumstances, therefore, it cannot be expected that appellant has to declare the same margin of profit in each year. The rejection of books of accounts can be made under section 145(3) of the Act where the AO is not satisfied about the correctness and completeness of the accounts of the assessee or where the assessee has not followed the method of accounting regularly and consistently, then the AO may compute the income/ loss of the assessee per the material available on record. In the present case of the appellant, the AO has not recorded any finding which could reflect that he is not satisfied about the correctness and completeness of the accounts of the appellant. Further, on perusal of various replies filed by the appellant it is noticed that details have been filed with respect to the sale, purchase, closing stock and expenses along with documentary evidences i.e. all factors affecting the net profit. Also there is no finding of the AO that the appellant has deviated from the method of accounting regularly followed by it. In these circumstances, I am of the considered view that AO was not justified in rejecting the books of accounts of the appellant. Hence, the rejection of books of account made by the AO is rejected and this ground of appeal of the appellant is allowed."

8. Further, CIT(A) deleted the addition made by AO by arbitrarily computing Net Profit before remuneration @ 5.206% by holding as under;

"Further under the income tax Act the profit and gains from business and profession are taxed on actual basis. In other words, the profit and gain which has actually accrued to the assessee can only be taxed in the hands of the assessee. Accordingly, in the

instant case when the actual profit earned by the appellant is available, then there is no need to estimate the same on ad-hoc basis especially when there is no evidence of falsehood in the profit declared by the appellant. I am, therefore, of the considered view that when all the data and entries made in the profit and loss account and balance sheet were not found to be incorrect in any manner, there could not have been any other result except what has been shown by the appellant in the books of account. Therefore, the addition made by the AO on account of estimation of net profit rate @5.206% is hereby directed to be deleted and the ground is allowed."

9. However, aggrieved by the order of CIT(A), Revenue filed an appeal raising following grounds of appeal;

"1. On the facts and circumstances of the case, whether the Ld. CIT(A) has erred by holding that the AO was not justified in rejecting the books of accounts of the assessee by invoking provision of section 145(3) of the I.T. Act, 1961, in spite of following facts:-

(i) During the course of survey, discrepancies were noticed in stock and cash. Stock on physical verification was found excess by Rs. 2,20,00,120/- and cash on physical verification was found excess by Rs. 40,00,000/-.

(ii) The assessee has declared lesser commission income during the year under consideration as compared to earlier years income.

(iii) The assessee has inflated the expenses debited in profit and loss account during the year.

2. On the facts and circumstances of the case, whether the Ld. CIT(A) has erred by deleting the additions made by AO @ 5.206% on account of Net Profit.

3. On the facts and circumstances of the case, whether the Ld. CIT(A) has erred by deleting the additions made by AO of Rs. 2,05,29,361/- on account of Net Profit.

4. The appellant craves, leave to add, to alter or amend any ground of appeal raised above at the time of hearing."

10. Heard and perused the record. Ld. DR submitted that Ld. CIT(A) has not considered the detailed examination of circumstances of AO. However, ld. AR supported the findings of Ld. CIT(A). The resultant findings on the grounds is as follows.

11. It is pertinent to observe from the record and submissions that;

i. The assessee has duly followed mercantile system of accounting throughout the year and has prepared books of account duly adhering to the accounting standards. Such books of accounts have also been duly audited by the Statutory Auditor.

ii. The assessee firm is also subject to Tax Audit and no adverse remarks have been made by the Tax Auditor of the assessee.

iii. The assessee has furnished ledger accounts of the expenses, details of sundry creditors along with their confirmations, details of partners, TDS certificates, Certificate of interest issued by bank, complete details of donations made and all other documents as & when asked for by the AO to support the authenticity and accuracy of the books of accounts of the assessee firm.

iv. AO has failed to point out a single defect in the documents furnished by the assessee or the books of accounts of the assessee.

v. No defect has been pointed out in the purchases or closing stock or creditors or debtors reported by the assessee.

vi. Each and every observation of the AO has not only been answered but also supported by the requisite documents.

vii. It is not the case of the AO that any inconsistency or contradiction has been observed in the books of accounts of the assessee.

12. In light of all of the above, we are of considered view that there is no error in the findings of Ld. CIT(A) that the books of accounts were rejected without cogent reasons. There is no allegation of change of any accounting practice by the assessee. There was no enquiry about the transactions reported in financials to corroborate there was any significant irregularity which made books inaccurate. It is a settled law held that in the absence of any material pointing towards falsehood of the books of accounts and no particular defect or discrepancy being pointed in the books of accounts, resort could not be made to rejecting the books of accounts by invoking Sec. 145(3), specially where same were duly audited by a statutory auditor. Reliance is rightly placed by Ld. AR on the following judicial pronouncements in this regard :

- The Pr. Commissioner of Income Tax-17 versus Time & Space Haulers, 2018 (7) TMI 1997-Bombay High Court, Dated 4.7.2018
- The Commissioner of Income Tax Versus Om Overseas, Shiv Nagar 315 ITR 185 High Court Punjab and Haryana
- Assistant Commissioner of Income Tax, Raipur versus Roopchand Tharani, 2011(11) TMI 426-Chhattisgarh High Court, Dated 1.11.2011
- Madnani Constructions Corporation P. Ltd. Versus Commissioner of Income-Tax, 2006 (12) TMI 79-Gauhati High Court, Dated – December 5, 2006

13. Further, it is a settled law, as cited by Ld. AR, that merely because the Net Profit has declined, the AO cannot resort to rejecting the books of accounts. Reliance is rightly placed on the following judicial pronouncements in this regard:

- The Pr. Commissioner of Income Tax-9 Versus IBILT Technologies Ltd. 2018(10) TMI 63-Delhi High Court, Dated – 12-09-2018.
- CIT versus Winner Constructions Pvt. Ltd., 2012 (5) TMI 394-Delhi High Court, dated- May 3, 2012
- Commissioner of Income Tax-XII versus Smt. Poonam Rani, 2010 (5) TMI 57-Delhi High Court, wherein the court held as under

“8. The fall in gross profit ratio, in the absence of any cogent reasons could not, by itself, have been a ground to hold that proper income of the assessee cannot be deduced from the accounts maintained by her and consequently, could not have been a ground to reject the accounts invoking Section 145(3) of the Act.

14. The discretion exercised about how much remuneration shall be paid to the partners is upon the discretion of the assessee firm cannot be basis to doubt the net profit itself. It is a settled position of law that revenue cannot sit into the armchair of the businessman and question the reasonableness of expenditure. Reliance is rightly by Ld. AR placed on the following judicial pronouncements in this regard:

- SA Builders Ltd. Versus Commissioner of Income Tax, 2006(12) TMI 82-Supreme Court, Dated : December 14, 2006
- Commissioner of Income Tax Versus Dalmia Cement (Bharat) Ltd. , 2001(9) TMI 48-Delhi High Court, Dated : September 4, 2001

15. We are of considered view that ad-hoc addition of Net Profit has not been sustained by Ld. CIT(A) on the basis of additional evidences before it. We are of considered view that prudent approach is needed to examine the explanation given by an assessee for decline in profits and statistical examination of financial of past years alone cannot be basis of gearing up the Net Profit. Ld. CIT(A) has appreciated the transactions leading to lower Net

profit and accepted explanation of assessee for fall in Net Profit while Ld. AO had examined the issue only on statistical parameters, which is not sustainable. The grounds raised by Revenue have no substance. **The appeal of Revenue is dismissed.**

Order pronounced in the open court on 10th October, 2023.

Sd/-

(N.K.BILLAIYA)

ACCOUNTANT MEMBER

Date:- 10.10.2023

Binita, SR.P.S

Copy forwarded to:

1. Appellant
 2. Respondent
 3. CIT
 4. CIT(Appeals)
 5. DR: ITAT
- AR, ITAT

Sd/-

(ANUBHAV SHARMA)

JUDICIAL MEMBER

New Delhi