

IN THE INCOME TAX APPELLATE TRIBUNAL
“H” Bench, Mumbai
Before S/Shri B.R. Baskaran (AM) & Ramlal Negi (JM)

I.T.A. No. 7048/Mum/2013
(Assessment Year 1999-2000)
I.T.A. No. 7049/Mum/2013
(Assessment Year 2003-04)
I.T.A. No. 7050/Mum/2013
(Assessment Year 2004-05)

M/s. Hindustan Organic Chemical Ltd. Harichandrai House 81, M.K. Road Marine Lines Mumbai-400 002. (Appellant)	Vs.	ACIT, Circle-4(2) Mumbai (Respondent)
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I.T.A. No. 6944/Mum/2013
(Assessment Year 1999-2000)
I.T.A. No. 6945/Mum/2013
(Assessment Year 2003-04)
I.T.A. No. 6946/Mum/2013
(Assessment Year 2004-05)

ACIT, Circle-4(2) Mumbai (Appellant)	Vs.	M/s. Hindustan Organic Chemical Ltd. Harichandrai House 81, M.K. Road Marine Lines Mumbai-400 002. (Respondent)
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PAN No.AAACH2663P

Assessee by	Shri K. Gopal & Shri Jitendra Singh
Department by	Shri Rahul Raman & Amit Kumar Singh
Date of Hearing	29.2.2016
Date of Pronouncement	20.5.2016

ORDER

Per Bench :-

These cross appeals relate to A.Ys. 1999-2000, 2003-04 & 2004-05 and all of them relate to the penalty levied u/s. 271(1)(c) of the Act. The penalty

levied by the Assessing Officer, having been deleted by Ld CIT(A) partly, both the parties have filed these appeals before us.

2. The assessee is a Government of India undertaking and is engaged in the business of manufacturing of basic chemicals and chemical intermediates.

3. We shall now take up the appeals filed for A.Y. 1999-2000. In this year the Assessing Officer levied penalty in respect of following four disallowances:-

- (i) Addition of Depreciation relating to decapitalised value of assets - Rs. 44,34,346/-
- (ii) Disallowance of Depreciation on plants, which are not on active use - Rs. 29,08,253/-.
- (iii) Addition relating to Valuation of closing stock of Eutectic Oil - Rs.13,00,000/-
- (iv) Disallowance of Prior period expenses - Rs. 78,01,000/-

4. In the appeal filed by the assessee, Learned CIT(A) deleted the penalty levied on the disallowance of prior period expenses and confirmed the penalty levied on the remaining three items. The assessee is in appeal challenging the confirmation of penalty and the revenue is in appeal challenging the deletion of penalty.

5. The first item on which the penalty was levied relates to the addition of depreciation relating "decapitalised" value of assets. Facts relating to the same are stated in brief. The assessee had built capital assets during the period from 1991 to 1998. During that period, it had capitalised the value of assets built by it. It is stated that some of the bills were accounted on provisional basis as per the assessment of the Management. It is pertinent to note that as per the accounting principles the assessee was required to make provision for known liabilities on estimated basis, if the concerned bills have not been received. During the financial year 2002-2003, the assessee reviewed its outstanding liabilities and the management decided that the liabilities to the tune of Rs.543.50 crores have become time barred. The Management took that view, since it found that there are no dues remaining to be paid on account of

assets capitalized and there are no known creditors to whom these liabilities can be associated. Since these liabilities have been created towards the assets capitalised in the earlier years, the assessee decided to decapitalise the same. The assessee noticed that it had already accounted for depreciation for an aggregate amount of Rs.209.31 lakhs in its books of accounts against the above said amount of Rs.543.50 lakhs. Accordingly the assessee credited a sum of Rs.209.31 lakhs to the profit and loss account and reduced the value of assets to the tune of Rs.334.19 crores. The aggregate amount of both adjustments amounting to Rs.543.50 lakhs was reduced from the liabilities account. All these accounting adjustments were made in Financial Year 2002-03 relevant to the assessment year 2003-04. It is pertinent to note that the assessee did not make corresponding adjustments to the depreciation schedule in its Income tax computation.

6. The Assessing Officer ordered for a special audit u/s. 142(2A) of the Act during the course of assessment proceedings relating to AY 2003-04. The special auditor expressed the view that the aggregate amount of depreciation of Rs.44.34 lakhs claimed by the assessee up to A.Y. 1999-2000 on the amount of Rs.543.50 lakhs should be taxed in A.Y. 1999-2000 itself. The AO was also concurred with that view. However, the assessee submitted that the assessing officer has already assessed a sum of Rs.487.38 lakhs relating to reversal of liabilities in AY 2003-04 itself and accordingly submitted that the addition of Rs.44.34 lakhs would amount to double addition. Hence the Assessing Officer added the above said amount of Rs. 44.34 lakhs on protective basis in AY 1999-2000. In the appellate proceedings relating to AY 1999-2000, the Learned CIT(A), however, confirmed the addition of depreciation of Rs.44.34 lakhs on substantive basis with the observation that deduction of corresponding amount may be given in A.Y. 2003-04.

7. In the penalty proceedings, the assessee submitted that the decapitalisation has taken place in F.Y 2002-03 and the depreciation for AY 1999-2000 was claimed on the basis of block of assets available in that year.

The AO was not convinced with that explanation and accordingly levied penalty u/s. 271(1)(c) of the Act on the above said amount and the same was also confirmed by learned CIT(A).

8. We have heard the parties on this issue. The Learned counsel appearing for the assessee submitted that the assessee has furnished all the particulars relating to decapitalisation in its books of account relating to F.Y. 2002-03. He submitted that the assessee has passed due accounting entries in that year. However, the AO has decided to add a sum of Rs. Rs. 44.34 lakhs, being the amount of depreciation relating to the period from 1991 to 1998 on protective basis in AY 1999-2000, but the Ld CIT(A) has added the same on substantive basis. He submitted the above said amount has already been added by the AO in 2003-04, but the tax authorities have only changed the assessment year and assessed the same in AY 1999-2000.

9. On the contrary, learned Departmental Representative placed heavy reliance on the order passed by learned CIT(A) on this issue. He submitted that the assessee has claimed excessive depreciation by inflating the value of its capital assets.

10. Having heard the rival submissions, we are of the view that there is merit in the contentions of the assessee. We notice that the assessee has voluntarily decapitalised the assets by examining its liabilities position in AY 2003-04. The undisputed fact remains that the assessing officer has added the liabilities reversed by the assessee to the total income of the assessee in AY 2003-04. The amount of Rs.44.34 lakhs is already included in the amount assessed in AY 2003-04, meaning thereby the tax authorities have only changed the year of assessment in respect of the amount of Rs.44.34 lakhs. Even though the assessee has not carried out necessary adjustments in he Income tax depreciation schedule in AY 2003-04, in our view, the concealment, if any, has to be examined only in that year. Accordingly, we are of the view that the addition made by changing the assessment year will not result either

in concealment of particulars of income or furnishing of inaccurate particulars of income. Accordingly we set aside the order of learned CIT(A) on this issue and direct the Assessing Officer to delete the penalty levied on the above said amount.

11. The next issue on which the penalty u/s. 271(1)(c) of the Act was levied relates to the addition on account of valuation of Eutectic Oil. The assessee had held stock of 650 MT of Eutectic Oil for the past several years. Over the years, the assessee considered the market value of the same as nil, as the same remained as a non-movable item and was lying with the assessee for the past several years. However, the Assessing Officer noticed that the assessee has sold the same @ Rs. 4000 per metric ton during the financial year relevant to A.Y. 2003-04. Accordingly he took the view that the valuation of the oil at NIL was not correct and accordingly he estimated the value of Eutectic Oil as on 31.3.1999 at Rs.2000/- per metric ton. Accordingly he valued the closing stock of oil at Rs.13 lakhs and added the same to the income of the assessee. The Assessing Officer also levied penalty on the above said addition and learned CIT(A) also confirmed the same.

12. Learned counsel submitted that the assessee has duly disclosed availability of Eutectic Oil in his books of account. It has also justified in valuing the same at nil value as it remained as non-moveable item for the past several years. He submitted that the assessee was making efforts to sell of the same in the market and finally it found an ex-employee who purchased the same @ Rs. 4000 per metric ton in the year relevant to A.Y. 2003-04. He submitted that sales amount realised by it has been duly offered as income in A.Y. 2003-04. The Learned AR submitted that the assessee has consistently taken the market value of Oil as nil over several years. Learned counsel submitted that the Assessing Officer, having decided to attribute certain value to the closing stock of oil, should have also valued the opening stock of oil at the same value, in which case, the addition would have been neutral. He submitted that the assessee had furnished proper explanations for taking the

closing stock value of Oil as NIL and further the assessee has furnished all the details relating to the closing stock of oil. Accordingly, the learned AR contended that the tax authorities are not justified in levying penalty.

13. We have heard learned Departmental Representative on this issue and perused the record. We notice that the assessee has been declaring the market value of this Eutectic Oil at nil for the past several years. However, the Assessing Officer has chosen to estimate the closing stock value of Eutectic Oil and has made the addition of Rs.13.00 lakhs. As pointed out by Ld A.R, he did not estimate the value of opening stock of oil, even though the oil stock was available as opening stock also. We also find merit in the submissions of the assessee that the amount realised by the assessee after expiry of four years cannot be a ground to disturb the closing stock value estimated by the assessee, particularly when the assessee is valuing the Eutectic Oil stock as nil for past several years. It is not shown by the AO that the assessee did not have any basis for valuing the oil stock at NIL value. Even otherwise, we notice that the assessee has offered proper explanations in this regard and it is not the case of the Assessing Officer that the assessee has concealed particulars relating to Eutectic Oil stock. Accordingly we find merit in the contentions of the assessee that the addition made by the Assessing Officer on estimated basis would not give rise to penalty u/s. 271(1)(c) of the Act. Accordingly we set aside the order of learned CIT(A) passed on this issue and direct the Assessing Officer to delete the penalty levied thereon.

14. The next issue relates to penalty levied on disallowance of depreciation on plant not put to use. Learned Counsel submitted that the Assessing Officer has listed out certain plants and disallowed depreciation claimed thereon by holding that they were not put to use and they have been held for disposal only. Learned Counsel submitted that after introduction of block concept of depreciation, individual assets lose their identity and hence the Assessing Officer was not justified in disallowing the depreciation by listing out certain plants. Accordingly, learned AR submitted that the disallowance of

depreciation made by the Assessing Officer is not justified on merits also. He submitted that the assessee has furnished all relevant details relating to the depreciation claimed by the assessee and it has neither concealed any particulars of income nor furnished any inaccurate particulars of income. Accordingly he contended that the penalty levied on the disallowance of depreciation was not justified.

15. We have heard learned Departmental Representative on this issue and perused the record. From the orders passed by the tax authorities we notice that the Assessing Officer has culled out details of plant not in use from the books of account maintained by the assessee, which shows that the assessee has not concealed any particulars of income or furnished any inaccurate particulars of income. There is merit in the contentions of the assessee that the assets shall lose their individual identity once it enters the block. Otherwise also, we notice that the assessee has offered explanations as to why it was constrained to claim depreciation on these assets. Thus we notice that the disallowance of depreciation claimed on assets, which had already lost their individual identity by entering into the block, is a debatable issue. Hence we are of the view that the assessee cannot be levied with the charge of concealment of particulars of income or furnishing any inaccurate particulars of income in respect of this addition. Accordingly, we set aside the order of learned CIT(A) on this issue and direct the Assessing Officer to delete the penalty relating to this addition.

16. We shall now take up the appeal filed by the Revenue. The penalty levied on addition relating to prior period expenses was deleted by learned CIT(A) on the reasoning that there is some merit in the contentions of the assessee that it claimed the same on the plea that they have got crystallised during the year under consideration. The Ld CIT(A) also noticed that the year of claim has only changed. On the contrary the Assessing Officer had disallowed the same as he took the view that these expenses do not relate to year under consideration.

17. We have heard the parties on this issue. We noticed that learned CIT(A) has given a finding that the claim made by the assessee was not an ingenuine claim and it is a case of postponement of claim only. The Learned CIT(A) has also taken note of the submissions made by the assessee that these expenses got crystallised during the year under consideration. Hence there is merit in the view taken by Ld CIT(A) that it is a case of mere change of accounting year in which expenses should be claimed and hence this issue becomes a debatable issue. It is well settled proposition of law that penalty u/s. 271(1)(c) of the Act cannot be levied on debatable issue. Accordingly we do not find any infirmity in the decision of learned CIT(A) in deleting the penalty levied on this addition.

18. We shall now take up the appeals relating to AY 2003-04. The AO levied penalty on the following additions made by him:-

- (i) reversal of excess liabilities of Rs. 4,87,38,201/-
- (ii) prior period expenses of Rs. 1,10,19,632/-
- (iii) stock of Eutectic oil of Rs. 12,70,000/- -
- (iv) disallowance u/s. 43B - Rs. 76,17,656/-
- (v) Loan & advances written off of Rs. 6,35,000/-
- (vi) depreciation on research & development equipment of Rs. 8,18,57,646/-
- (vii) depreciation on stores and spares of Rs. Rs. 47,46,477/-
- (viii) Disallowance u/s. 145A of Rs. 87,83,980/-

The Ld CIT(A) deleted the penalty pertaining to (ii), (iii) and (viii) referred above and confirmed the penalty in respect of remaining additions. Both the parties have filed appeals challenging the decision of Ld CIT(A).

19. The first issue relates to the penalty levied on the addition relating to reversal of excess liabilities. This addition relates to the decapitalisation of assets, which was discussed in the preceding paragraphs while dealing with the appeal of the assessee relating to AY 1999-2000. It is pertinent to note

that the assessee has carried out necessary adjustments in its books of accounts only. It did not make any disclosure in the income tax computation, by way of adjustment of value of block of assets and also did not offer the amount of depreciation written back it for taxation. The assessee has simply explained that it could not identify the values under the block concept.

20. We heard the parties on this issue. The Ld A.R reiterated the submissions made before the tax authorities and the Ld D.R supported the orders passed by them. The fact remains that the assets to the extent of Rs.543 lakhs were not created at all by the assessee and the said fact was found by it only in FY 2002-03. This situation occurred, since it has been accounting for the assets on estimated basis. The principle of individual assets losing their identity, in our view, shall apply only to the existing assets, whether tangible or intangible. Here is a case, where the value of assets have been inflated and, in our view, the above said principle cannot be applied to the inflated portion of the value of the assets. Having identified the inflated value and having passed necessary entries in the books of account, in our view, the assessee should have disclosed these facts and should have offered the depreciation amount, which was claimed wrongly.

21. We notice that the assessing officer has assessed the entire amount of liability reversed by the assessee as the income of the assessee. By making certain adjustments, he has determined the addition at Rs.487 lakhs and the Ld CIT(A) has given further relief to the extent of Rs.44.34 lakhs directed by him to be assessed in AY 1999-2000. Since the liabilities relate to the capital assets, the question as to whether such kind of liabilities can be assessed as income of the assessee u/s 41(1) shall become a debatable one. Accordingly, we are of the view that the penalty cannot be levied on the capital portion of the reversed liability and the same should be restricted to the depreciation portion alone. Accordingly, we modify the order of Ld CIT(A) on this issue and direct the AO to restrict the penalty on the addition relating to depreciation portion alone, which was claimed by the assessee over the years.

22. The next issue relates to the penalty levied on addition relating to closing stock value of Eutectic Oil - Rs.12,70,000/-. The details relating to valuation of Eutectic oil was discussed in the preceding paragraph while dealing with the appeal of the assessee relating to AY 1999-2000. In this year, the assessee has sold a portion of the oil at Rs.4,000/- per MT. Thus, the claim of the assessee, that it did not have any market value has been disproved in this year. However, the assessee has chosen to declare the market value as NIL. Hence, the explanation of the assessee stands disproved by the facts available in its records itself. Accordingly, we are of the view that the Ld CIT(A) was justified in confirming the penalty levied on this addition.

23. The next issue relates to the penalty levied on the Disallowance of loans and advances written off – Rs.6,35,000/-. The assessee had accounted for amounts receivable from the nearby villages towards water charges, electricity etc. Since the assessee could not realise the same over the years, it wrote off it as bad debts. The AO disallowed the same with the reasoning that the assessee has not produce any evidence to show that the debt has actually become bad. The Ld CIT(A) also confirmed the same. We heard the parties on this issue. The question as to whether debt has become bad or not, is a debatable issue. The Ld A.R also contended that there is no requirement of proving that the debt has become bad, after the amendment made in sec. 36(1)(vii) of the Act. Hence, we are of the view that the penalty could not be levied on debatable issue. Accordingly, we set aside the order passed by Ld CIT(A) on this issue and direct the AO to delete the penalty levied thereon.

24. The next issue relates to the penalty levied on the disallowance of depreciation claimed on Research and Development equipment. The AO disallowed the claim on the reasoning that the assessee had claimed entire expenditure as deduction u/s 35(1)(iv) of the Act. Accordingly he disallowed the depreciation amount relatable to R & D equipments and levied penalty thereon. Before Ld CIT(A), the assessee submitted that it had included the value of R & D equipments as part of block, but did not claim depreciation at

all. Accordingly, the Ld CIT(A) directed the AO to verify the contention of the assessee and delete the penalty, if the assessee's claim is found to be correct. Since the issue is restored back to AO to verify the claim of the assessee, we do not find any infirmity in it.

25. The next issue relates to the penalty levied on the disallowance of depreciation on stores and spares- Rs.47.46 lakhs. The Ld CIT(A) has confirmed the penalty levied on the above said item without discussing the same. However, we notice that the assessee has capitalised certain stores and spares and accordingly claimed depreciation thereon. The question as to whether the assessee could capitalise its stores and spares is a debatable issue and hence the disallowance of depreciation claimed thereon also becomes debatable one. Accordingly, we set aside the order of Ld CIT(A) passed on this issue and direct the AO to delete the penalty levied on this addition.

26. We shall now take up the appeal filed by the revenue for AY 2003-04. The first issue relates to the penalty levied on disallowance of prior period expenses. Identical issue was considered by us in the preceding paragraphs while dealing with the appeal filed by the revenue for AY 1999-2000. Consistent with the view taken therein, we confirm the order of Ld CIT(A) on this issue.

27. The next relates to the penalty levied on the disallowance made u/s 43B of the Act. The AO disallowed the payments made towards P.F, ESI etc. beyond the due date prescribed in the respective Act, but within the grace period specified therein. It is the case of the assessee that the payment made within the grace period should also be considered as the payment made within the statutory period. We are of the view that this issue is debatable one and hence the penalty cannot be levied on this addition. Even otherwise, this addition has been made on account of statutory fiction and it is not the case of the AO that the assessee has concealed any particulars of income. Hence we confirm the order passed by Ld CIT(A) on this issue.

28. The last issue contested by revenue relates to the penalty levied on the addition made u/s 145A of the Act. Similar additions were made in the earlier years and they were deleted by the Ld CIT(A). In this year, the assessee has inadvertently omitted to contest this addition before Ld CIT(A) and accordingly it came to be confirmed. The AO examined the value of closing stock and took the view that the assessee has not loaded direct expenses to the value of raw materials. Accordingly he estimated the value of direct expenses at 2% of the cost of raw materials and accordingly added the same. In the earlier years, the assessee demonstrated before the Ld CIT(A) that the valuation of raw materials did include the proportionate amount of direct expenses. Accordingly, the Ld CIT(A) deleted identical additions made in the earlier years. Since the facts are identical and since the AO has made the addition on estimated basis, we are of the view that the Ld CIT(A) was justified in deleting the penalty levied on this addition, even though the assessee has accepted the addition by not contesting the same.

29. We shall now take up the appeals filed by both the parties for AY 2004-05. The penalty was levied on the following additions:-

- (i) depreciation allowance on account of decapitalisation of assets of Rs. 10,52,291/-
- (ii) prior period expenses of Rs. 1,10,49,240/-
- (iii) valuation of Eutectic Oil at Rs. 10,87,068/-
- (v) Disallowance u/s. 43B of Rs. 44,37,656/-

The Ld CIT(A) confirmed the additions listed as (i) and (iii) and deleted the penalty in respect of remaining two items.

30. In respect of addition relating to depreciation claimed on decapitalisation of assets, we have held in AY 2003-04, the penalty is leviable on the depreciation portion of the liabilities reversed by the assessee. Accordingly, we direct the AO to examine this addition in the light of discussions made by us in

the preceding paragraph while dealing identical issue in AY 2003-04. The order of Ld CIT(A) stands modified accordingly.

31. In respect of valuation of Eutectic oil, we are of the view that the penalty could be levied on the net addition, i.e., the difference between the opening stock and closing stock. Accordingly we direct the AO to give credit for opening stock of the oil and levy penalty on the net addition, if any. The order of Ld CIT(A) stands modified accordingly.

32. The revenue is contesting the decision of Ld CIT(A) in respect of additions relating to Prior period expenses and disallowance u/s 43B of the Act. Identical issues were considered by us in the preceding paragraphs while dealing with the appeal of the revenue relating to AY 2003-04. Consistent with the view taken therein, we confirm the order passed by Ld CIT(A) on both these issues.

33. In the result, all the appeals of the revenue are dismissed and the appeals of the assessee for AY 2003-04 and 2004-05 are partly allowed. The appeal of the assessee for AY 1999-2000 is allowed.

Order has been pronounced in the Open Court on 20.5.2016.

Sd/-
(RAMLAL NEGI)
JUDICIAL MEMBER

Sd/-
(B.R.BASKARAN)
ACCOUNTANT MEMBER

Mumbai; Dated : 20/5/2016

Copy of the Order forwarded to :

1. The Appellant
2. The Respondent
3. The CIT(A)
4. CIT
5. DR, ITAT, Mumbai
6. Guard File.

//True Copy//

BY ORDER,

(Dy./Asstt. Registrar)
ITAT, Mumbai

PS