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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**
+ ITA 995/2018

Date of decision : 12th September, 2018

THE PR. COMMISSIONER OF INCOME TAX-9.....Appellant

Through: Mr. Ruchir Bhatia, Advocate

versus

IBILT TECHNOLOGIES LTD. Respondent

Through

CORAM:

HON'BLE MR. JUSTICE SANJIV KHANNA

HON'BLE MR. JUSTICE CHANDER SHEKHAR

SANJIV KHANNA, J.(ORAL):

This is a peculiar case where the Assessing Officer had primarily rejected the book results declared by M/s IBILT Technologies Ltd. (respondent-assessee) for the Assessment Year 2007-08 on the ground that there was net loss of Rs.16.41 lacs, compared to net profit of Rs. 1.34 crores in the Assessment Year 2006-07. The explanation given by the respondent-assessee to justify and explain the book results for the Assessment Year 2007-08 were rejected with a simple observation that the explanation was not found to be complete and satisfactory. The Assessing Officer recomputed the taxable income at Rs. 2,13,72,000/- by applying gross profit ratio of 4%.

2. The Commissioner of Income Tax (Appeals) had noted detailed submissions made by the respondent-assessee to explain and elucidate the reason why there was a loss in the said year. For the sake of completeness, we would refer to the said submissions, which have been noted by the Commissioner of Income Tax (Appeals) in tabular form:-

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| S. No. | Observations made by Ld. AO | Our submission | Remarks |
|--------|-----------------------------|---|---------------|
| 1. | The assessee was | Specific factors which caused loss of Rs. 16,41,966 during | Therefore the |



| | specifically asked to explain the reason for fall in profitability` | <p>A.Y. 2007-08 against the profit of Rs. 1,34,71,291 during previous A.Y. 2006-07</p> <p>The financial year 2006-07 (relevant year for the A.Y. 2007-08) was very tough year for the company. During this year the company has achieved a turnover of Rs. 53.43 crores against the turnover of Rs. 34.36 crores in the immediate preceding year 2005-06 registering a huge growth of 52% over the previous year. This phenomenal has put pressure on the margins of the company as more infrastructure, working capital & men power was required to achieve this. However the company <u>somehow maintained the operating margins</u> but could not prevent losses due to the reasons/factors explained here above. A summary of the major factors which caused dentin the profitability of the company during the year is given hereunder:</p> | <p>surprise contention the Ld AO that the company shown profit last year and loss in current year is not justified.</p> <p>We are relying on the follow judgments: Sh. Pyare Lal Mittal V/s ACIT (2007) 197 Taxation 186 (Gauhati)</p> <p>Dhakeshwari Cotton Mills V/s. CIT 26 ITR 775 (SC)</p> <p>Puspanjali Dying & Printing Mills (P) Ltd. 72 TTJ 886 (AHD)</p> | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
|-------|---|--|--|------------------|----------|----------|------------------|---|--------------|------------|------------|-----------|---|--------------|------------|------------|-----------|---|--------------|------------|-----------|-----------|---|-------------------------------------|--------------|------------|-------------|---|--|--------------|--------------|--------------|---|------------|-------------|------------|--|---|
| | | <table border="1"> <thead> <tr> <th>Sl no</th> <th>Particulars</th> <th>AY 07-08</th> <th>AY 06-07</th> <th>Impact on profit</th> </tr> </thead> <tbody> <tr> <td>1</td> <td>Other income</td> <td>12,013,931</td> <td>15,488,789</td> <td>3,474,858</td> </tr> <tr> <td>2</td> <td>Depreciation</td> <td>32,386,450</td> <td>24,519,921</td> <td>7,866,529</td> </tr> <tr> <td>3</td> <td>Finance cost</td> <td>11,337,894</td> <td>8,648,891</td> <td>2,689,003</td> </tr> <tr> <td>4</td> <td>Payment to & provision for employee</td> <td>14,53,39,492</td> <td>1293, 9271</td> <td>3,24,00,221</td> </tr> <tr> <td>5</td> <td>Cost of service, administration & selling expenses</td> <td>35,89,83,398</td> <td>19,94,81,710</td> <td>15,95,01,688</td> </tr> <tr> <td>6</td> <td>Net profit</td> <td>(1,641,966)</td> <td>13,471,291</td> <td></td> </tr> </tbody> </table> <p>From the above table, it is clear that the above factors have caused a huge reduction in profit for the year.</p> | Sl no | Particulars | AY 07-08 | AY 06-07 | Impact on profit | 1 | Other income | 12,013,931 | 15,488,789 | 3,474,858 | 2 | Depreciation | 32,386,450 | 24,519,921 | 7,866,529 | 3 | Finance cost | 11,337,894 | 8,648,891 | 2,689,003 | 4 | Payment to & provision for employee | 14,53,39,492 | 1293, 9271 | 3,24,00,221 | 5 | Cost of service, administration & selling expenses | 35,89,83,398 | 19,94,81,710 | 15,95,01,688 | 6 | Net profit | (1,641,966) | 13,471,291 | | <p>Raghubar Mandai Harihar Mandai VIs State of Bihar 8 STC 770(SC)</p> <p>Aluminium Industries (P) Ltd. V/s CIT GLR 216 (GAU) Calcutta Discount Pvt. Ltd. v/s 91 ITR 8 (SC)</p> |
| Sl no | Particulars | AY 07-08 | AY 06-07 | Impact on profit | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 1 | Other income | 12,013,931 | 15,488,789 | 3,474,858 | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 2 | Depreciation | 32,386,450 | 24,519,921 | 7,866,529 | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 3 | Finance cost | 11,337,894 | 8,648,891 | 2,689,003 | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
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| 5 | Cost of service, administration & selling expenses | 35,89,83,398 | 19,94,81,710 | 15,95,01,688 | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
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| | | <p>Also we are enclosing comparative chart for the Assessment years 2004-05, 2005-06, 2006-07, 2007-08 & 2008-09 showing net profit & turnover.</p> <p style="text-align: center;">Refer Annexure-1</p> | |
| 2 | <p>The reasons for non disclosure of quantitative stock details in tax audit report for the year under consideration and non existence of closing stock & WIP</p> | <p>The nature of business of the Company and the manner in which it is carried on by the Company is <u>very peculiar and different from other trading or manufacturing organizations.</u> Most of the purchases of IT equipments, software and license are from reputed OEMs (Original Equipments Manufacturers) and requirement of every client is unique since adoption of IT by the client is one time affair and must take care of its functionality, every purchase is a customized purchases rather than an <u>Off the Self</u> ready item, therefore as soon as the goods are delivered to the customers revenue is recognized and sales invoices are raised. In this process purchases and sales both take place at the same time and <u>question of closing stock & WIP does not arise.</u></p> <p>Also copies of tax audit reports by the statutory auditors of the company clearly mentioning the non existence of stocks are enclosed for the AY 2004-05, 2005-06, 2006-07, 2007-08 & 2008-09.</p> | <p>Therefore contention the Ld AO regarding and opening and closing stock are not correctly justified.</p> <p>We are relying on the following judgments with regards to consistency & continuity</p> <ol style="list-style-type: none"> 1. Radha Swami Satsang Vs. CIT. Supreme Court.100 CTR 267 2. CIT Vs. ARJ Security Prints High Court 183 CTR 323 3. CIT Vs. Neo Polypack Pvt. Ltd High Court 245 ITR 492 |
| | | <p>Also we are enclosing comparative chart for the above-mentioned Assessment years showing that there is no opening stock, closing stock & WPI. Refer Annexure-1</p> | |
| 3 | <p>Further on perusal of other income details disclosed by the assessee, it is seen that substantial amount of Rs.1.13 crores has been shown as <u>provisions written back</u> as against the corresponding amount of Rs. 1.46 crores disclosed in the last year.</p> | <p>During the course of the assessment, all the details of provision written back along with the nature of these provisions written back was filed with the Ld. AO. However it is reproduced again for your reference.</p> <p>The Company Ibilt has <u>acquired an Informatic Divison</u> (Division) of the company <u>M/s Crompton Greaves Ltd.</u> with the objective of consolidating similar types of business under one company effective from 1st July 2005. Sales consideration as agreed between the parties was Rs. 100 lacs. Apart from the sale consideration, Ibilt has agreed <u>to take over future liabilities of the Divison towards unexpired warrant and AMC.</u> These future liabilities were valued at Rs. 265 lacs and</p> | <p>Therefore the contention of the Ld AO is justified in the eyes of the law</p> |



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| | | a provision for such future liabilities was created in the books of account. | |
| | Such a scenario remains incomprehensible as to why this situation would arise in the case of the assessee which is purely working on <u>order to order basis</u> and is stated by the Assessee himself to have nil stock in its books at the end of the financial year. In response to the specific query given on this issues the submission made by the assessee was not found to be complete and satisfactory. He could not bring on record the exact details of the amounts written back by the assessee and the purpose thereof. I am of the firm view that the assessee has failed to bring on record the real facts pertaining to the matter under consideration. | <p>In subsequent years, expenses incurred/paid against this provision were debited to the provision account since these expenses were part of sale consideration.</p> <p>As per accounting practices, these expenses should be debited to respective expenses heads of accounts and corresponding amount should be transferred from provision account and to be shown as provision written back in the Profit & Loss account.</p> <p>In nutshell provision written back is an item against which expenses have been incurred/paid and debited to profit and loss account and corresponding amount has been transferred to Provision Written Back account from provision account and subsequently to Profit & Loss Account.</p> <p>The Ld AO was specifically requested vide letter dated 07.12.2009 that if anything still is required or to be explained. But the Ld AO kept mum and did not ask anything further. All the details for provision written back was filed with the Ld. AO at the time of assessment.</p> <p>However it is again attached herewith you for your kind reference. Refer Annexure-2</p> | |
| 4 | Assessee was further asked to <u>file details of foreign travel during</u> the period from 01.04.2006 to 31.03.2007 along with documentary evidences to establish the expenses so incurred was wholly and completely for business purposes. Details filed by the assessee were found to be incomplete since the assessee has no where mentioned the purposes for which traveling were under taken: | <p>Foreign travels were made for business purpose and all the details of foreign travel were filed with the Ld.AO along with the purpose for which it was made during the course of the assessment.</p> <p>The Ld AO was specifically requested vide letter dated 07.12.2009 that if anything still is required or to be explained. But the Ld AO kept mum and did <u>not ask anything further.</u></p> <p>However it is again attached herewith you for your kind reference. Refer Annexure-3</p> | Therefore the contention of Ld AO is justified in the eyes of the Law |
| 5 | It is further observed that the assessee has claimed <u>provision for doubtful advances of Rs.17,90,884/-</u> which has not been added back to the total income of the assessee, since the same represents <u>unascertained</u> | <p>a) Provision for doubtful advances of Rs. 17,90,884/- has not been added back to the total income of the assessee as it is a ascertained liability as explained below and not unascertained liability as mentioned by the Ld. AO.</p> <p>i) This ascertained provision has been made for amount due from employees (Rs. 429787/-) but not recoverable from them as <u>they have left the organization.</u> Refer Annexure-4</p> | The Ld AO was specifically requested vide letter dated 07.12.2009 that if anything still is required or to be explained. But the Ld. AO |



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| <p>liability. Considering all the above facts discussed above and the circumstances of the case. I am of the view that the assessee has failed in disclosing its true and correct income in its return filed in this office. The assessee has remained silent throughout the proceedings for the reasons for a fall in its profitability as a result of which the loss return has been filed. It may further be stated that in view of the fact that assessee enjoys a high profile clientless base the business can not have situation of loss in normal circumstances. Further it is again incomprehensible as to why assessee is showing loss in this year when there was profitability till last year. The assessee has not been able to justify this situation. In view of the facts as narrated above where true and fair picture of the assessee's accounts is not forthcoming provisions of Section 145 (3) of the Act are invoked and reject the results as shown by the assessee and estimate total income of the assessee on a very conservative basis at the rate of 4% of the total turnover which comes to Rs.2,13,72,000/-. This shall take care of the various specific disallowances as discussed above. The rate of 4% has been taken as the assessee has declared its NP @ 3.73% in the last year even with a lesser turnover.</p> | <p>This is also an ascertained liability and therefore specific provision has been made for it.</p> <p>ii) Provision was made for Rs. 1361096.90 in respect of amount due from the different parties but not recoverable from them. Refer. Annexure-4</p> <p>All the details for provision for doubtful advances was filed with the Ld.AO at the time of assessment.</p> <p>The Ld AO was specifically requested vide letter dated 07.12.2009 that if anything still is required or to be explained. But the Ld AO kept mum and did not ask anything further.</p> <p>However it is again attached herewith you for your kind reference.</p> | <p>kept mum and did not ask anything further. It seems that the Ld. AO found rejection of books of account easier than asking any further details and explanations. It seems that Ld. AO was determined to reject the books of account and to without giving proper opportunity to the assessee since no show cause was given to the assessee to explain "why books of accounts should not be rejected and assessee's total income should not assessed at 4% of the total turnover.</p> <p>Therefore, the contention of the Ld. AO is justified in the eyes of the Law.</p> <p>We are relying on the follow judgments:</p> <p>Sh. Pyare Lal Mittal V/s ACIT (2007) 197 Taxation 186 (Gauhati)</p> <p>Dhakeshwari Cotton Mills V/s.</p> |
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| 6 | Rejection of books of accounts u/s 145 (3) of the Act | | Therefore the contention of the Ld AO to reject the book of accounts and invoke the Sec145(3) is not justified. |
| S NO. | Observations made by Ld. AO | Our submission | Remarks |
| 1. | The assessee was specifically asked to explain the reason for fall in profitability | <p>Specific factors which caused <u>loss of Rs. 16,41,966</u> during A.Y. 2007-08 against the profit of Rs. 1,34,71,291 during previous A.Y. 2006-07</p> <p>The financial year 2006-07 (relevant year for the A.Y. 2007-08) was very tough year for the company. During this year the company has achieved a turnover of Rs. 53.43 crores against the turnover of Rs. 34.36 crores in the immediate preceding year 2005-06 registering a huge growth of 52% over the previous year. This phenomenal growth has put pressure on the margins of the company as more infrastructure, working capital & men power was required to achieve this. However the company <u>somehow maintained the operating margins</u> but could not prevent losses due to the reasons/factors explained here above. A summary of the major factors which caused</p> | <p>Therefore the contention the Ld AO that the company shown profit last year and loss in current year is not justified.</p> <p>We are relying on the follow judgments:</p> <p>Sh. Pyare Lal Mittal V/s ACIT (2007) 197</p> |



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|---|-------------------------------------|---|--------------|------------------|--|
| | | dentin the profitability of the company during the year is given hereunder: | | | Taxation 186 (Gauhati) Dhakeshwari Cotton Mills V/s. CIT 26 ITR 775 (SC) |
| Sl no | Particulars | AY 07-08 | AY 06-07 | Impact on profit | |
| 1 | Other income | 12,013,931 | 15,488,789 | 3,474,858 | |
| 2 | Depreciation | 32,386,450 | 24,519,921 | 7,866,529 | Puspanjali Dying & Printing Mills (P) Ltd. 72 TTJ 886 (AHD) |
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| 5 | Cost of service, administration | 35,89,83,398 | 19,94,81,710 | 15,95,01,688 | Aluminium Industries (P) Ltd. V/s CIT GLR 216 (GAU) |
| 6 | Net profit | (1,641,966) | 13,471,291 | | Calcutta Discount Pvt. Ltd, V/s 91 ITR 8 (SC) |
| <p>From the above table, it is clear that the above factors have caused a huge reduction in profit for the year.</p> <p>Also we are enclosing comparative chart for the Assessment years 2004-05, 2005-06, 2006-07, 2007-08 & 2008-09 showing net profit & turnover.</p> <p>Refer Annexure-1</p> | | | | | |

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3. It is not disputed and challenged that the respondent-assessee was engaged in supplying computer equipment, networking equipment and computer software on turnkey basis, primarily to government department/bodies and government companies. They were also providing warranty, annual maintenance contract and facility management services for up to five years. The contracts awarded to them



were on tender basis. Further, the respondent-assessee was purchasing equipments from reputed original equipment manufacturers (OEMs) like IBM, HP, ORACLE, Cisco, Dlink, Dax, Redhat, Acer, Sun etc. The assessment order states that there was exponential increase in the turnover from Rs.34.36 crore in the last year to Rs.53.43 crore in the current year, and the respondent-assessee had explained that to meet the commitments, they had recruited employees. The respondent-assessee had produced books of accounts including cash book and ledgers, going into nine volumes along with the vouchers. To justify and explain drop and decrease in operating profits the respondent-assessee had produced and furnished details as is apparent from the chart/table quoted above.

4. Learned counsel for the Revenue states that the respondent-assessee had not declared any opening and closing stock. He relies on the assessment order. However, the Assessing Officer did not examine and deal with the contention and plea raised by the respondent-assessee, duly taken into consideration by the Commission of Income Tax (Appeals), that supply orders were directly placed with the OEM, who had then made the supplies to the customers. Accordingly, the respondent-assessee did not keep or maintain stock-in-hand. In this manner, the respondent-assessee had cut down on their inventory costs, to ensure better profitability.

5. The Assessing Officer should have verified and examined the details of the purchases made and the supplies made, ascertaining whether or not there was any lapse in not declaring opening and closing stock. The books of accounts could not have been rejected on the ground that no opening or closing stock was declared, without the said exercise being undertaken.

6. The other reason given by the Assessing Officer to reject the books of accounts and make best judgment assessment was that the respondent-assessee had written back substantial amount of Rs.1.13 crore and had also claimed



provision for doubtful advances of Rs.17,90,884/-. The respondent-assessee had explained that they had acquired informatic division from M/s Crompton Greaves Ltd., with the objective of consolidating similar types of business under one company effective from 1.7.2005. As per terms, the respondent-assessee had agreed to take over future liability of the division towards unexpired warranty and the AMC. Clearly, the Assessing Officer did not consider the submission made and had failed to deliberate upon explanation given by respondent-assessee. With regard to the amounts written back, it was stated that these were expenses which had been incurred or paid and accordingly debited to the profit and loss account. Reference could be made to the chart/table reproduced above from the order of the Commissioner of Income Tax (Appeals).

7. Section 145 (2) of the Act empowers the Assessing Officer to make best judgment assessment when he is not satisfied with correctness or completeness of the accounts of the assessee. Best judgment assessment in terms of Section 145 can also be framed when no method of accounting has been regularly followed or where the method employed is such that the income, profit and gains cannot be properly deduced therefrom.

8. Books of accounts were not rejected by the assessing Officer as unreliable on the ground that transactions were omitted, proper particulars and vouchers were not forthcoming or there were inherent lacunas and other defects. The two/three feeble reasons given by the Assessing Officer for rejecting the book results have not been accepted by the appellate authorities. Reasons and explanation given by the respondent-assessee regarding opening/closing stock, amount written back etc. have been accepted. It is not the case that the method of accounting deployed was not regularly followed or it was not possible to deduce profit and gains from the method deployed. The Assessment Order is silent and



does not comment and state that the books of accounts were incomplete, incorrect or unreliable.

9. If there is fall in the gross profit ratio, reasons and grounds given by the respondent/assessee have to be examined objectively, fairly and in a non-partisan manner. Past results could be a good reason to conduct detailed verification, albeit would not be the only ground and reason to make addition by rejecting the books of accounts. Good and cogent reason why the financial results should be rejected has to be given. Books of accounts cannot be rejected as the respondent-assessee has suffered losses, where as in the immediate earlier year profit was made. Fall in gross profit ratio could be due to various reasons, and cannot be the sole and only ground to reject the book results in entirety and frame best judgment assessment [see *Commissioner of Income Tax-XII v. Poonam Rani (2010) 326 ITR 223*, *Action Electricals v. Deputy Commissioner of Income Tax (2003) 180 CTR 62*]. The reasoning given in the assessment order to compute income on hypothetical basis by applying gross profit ratio of 4% is completely fallacious, wrong and is contrary to well-settled law, as expounded vide judgments reported as *Commissioner of Income Tax, West Bengal v. Calcutta Discount Co. Ltd.*, (1974) 3 SCC 260, *Dhakeshwari Cotton Mills Ltd. v. Commissioner of Income Tax, West Bengal*, (1954) 26 ITR 775 (SC) and *Raghubar Mandal Harihar Mandal v. State of Bihar*, AIR 1957 SC 810.

10. The present appeal has no merit and the same is dismissed *in limine*.

SANJIV KHANNA, J

CHANDER SHEKHAR, J

SEPTEMBER 12, 2018/tp