

**IN THE INCOME TAX APPELLATE TRIBUNAL
AMRITSAR BENCH; AMRITSAR.**

BEFORE SH. T. S. KAPOOR, ACCOUNTANT MEMBER
AND SH. N. K. CHOUDHRY, JUDICIAL MEMBER

I.T.A. No. 53/(Asr)/2015

Assessment Year: 2009-10

PAN: AABFR1996F

M/s. Royal Wood Industries, 26/3, Phase-III, Industrial Area, Gangyal, Jammu. (Appellant)	Vs.	J. C. I. T., Range -1, Jammu. (Respondent)
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Appellant by : Sh. P. N. Arora (Adv.)

Respondent by: Sh. S. S. Kanwal (D. R.)

Date of Hearing: 05.10.2017

Date of Pronouncement: 04.12.2017

ORDER

PER T. S. KAPOOR (AM):

This is an appeal filed by assessee against the order of Ld. CIT(A), Jammu, dated 10.11.2014 for Asst. Year: 2009-10.

2. The assessee has taken the following grounds of appeal:

"1. That Ld. Commissioner of Income Tax (Appeals) was not justified in sustaining addition of Rs. 64,726/- on account of payments made for freight of goods to different drivers of trucks.

2. That Commissioner of Income Tax (Appeals) has not appreciated the fact that freight payments of Rs. 64,726/- were genuine payments and are being made to individual drivers of truck.

3. That the Ld. Commissioner of Income Tax (Appeals) was not justified in retaining addition of Rs. 5,27,503/- on account of investment in Building, discrepancies in stock and other deficiencies found at the time of survey.

4. That Ld. Commissioner of Income Tax (Appeals) was not justified in not deleting addition of Rs. 5,27,503/- which was not based on facts & not supported by documentary evidence.

5. *That Ld. Commissioner of Income Tax (Appeals) has not looked into facts of the case and has never called for the statement recorded by the assessee which is already with deptt.*
 6. *Ld. Commissioner of Income Tax (Appeals) contention about the valuation of closing stock is not correct & not based as facts as the closing stock is always to be valued at cost and not selling price.*
 7. *Ld. Commissioner of Income Tax is not correct in saying that no objections were raised while framing the valuation of damaged stocks and consumables.*
 8. *Ld. Commissioner of Income Tax (Appeals) has not appreciated the fact that the addition of Rs. 5,27,503/- represents cut pieces of finished goods, damaged stock and consumable stock which have been valued at selling price, but actually don't have any value."*
3. At the outset, the Ld. AR submitted that the payments amounting to Rs.64,726/- were made on 26.04.2008, 12.05.2008 and 14.07.2008 amounting to Rs.21730/-, 21590/- and Rs.21406/- respectively to drivers for transportation of goods. It was submitted that drivers of trucks were not known to assessee and they always insist on cash payments. It was submitted that genuineness of the payment has not been doubted as the purchases made by assessee has been accepted with the help of books of accounts. The Ld. AR submitted that it has been held by several courts that where the payments are genuine and identity of the payees is established, in that case the practicability has to be seen from the point of view of businessman and not from the point of view of tax collector and reliance in this respect was placed the decision of ITAT, Amritsar Bench, in the case of ITO, Jammu Vs. Sh. Atul Gupta Rajouri in ITA No. 465/Asr/2016. In view of above, it was argued that the addition confirmed by the Ld. CIT(A) may be deleted.

As regards the second addition of Rs.5,27,503/-, it was submitted that the survey was conducted on 15.02.2009 and the Assessing Officer found that there was a difference of Rs.527503/- on account of stock. It was explained that there was no such difference and the reasons were explained before the JCIT, Jammu in which it was submitted that stock in hand included inventory of consumable stock of Rs.111740/- which was directly booked in profit and loss account and this was done as per past practice followed by the assessee year to year.

As regards the other difference of Rs.12750/- on account empty drums, the Ld. AR submitted that these drums were at the premises of the assessee but these drums did not belong to assessee as these were returnable basis and had been received by assessee alongwith the chemicals and therefore no addition should have been made on account of this difference.

As regards the other addition on account of difference in stock of finished goods, the Ld. AR further submitted that Assessing Officer at the time of survey had valued the stock laying at the premises on the basis of selling prices which is not justified as the closing stock has to be calculated on the basis of cost price. The Ld. AR invited our attention to the inventory of stock of finished goods lying at page 25 and submitted that the ply of 4 mm/3 mm was valued at Rs.51.56 per sq. m. whereas its cost price was Rs. 40 and Rs.35 respectively as is apparent from the stock statement of finished goods placed at P.B. page 39. The Ld. AR

submitted that the stock as on 31.03.2009 as per the statement at page 39 has been accepted by the Assessing Officer during assessment proceedings. Therefore while finalizing the assessment, the Assessing Officer was bound to take these rates for the purpose of arriving at the difference in stock. The Ld. submitted that similarly the plys of 12mm and 9mm has been valued by the survey team at Rs.135 per sq. mm. whereas its price as per the stock statement was from Rs. 70 to 95. The Ld. AR further submitted that stock of finished goods placed at P.B. page 25 included damaged and cut pieces which was not saleable and its valuation was not taken into account in the opening stock as well as in the closing stock. Our attention was invited to P.B. 1 and 2 where copy of letter written to Assessing Officer explaining the difference in valuation of stock was placed.

In view of the above, it was argued that if the correct calculation based upon purchase prices as per the stock statement as on 31.03.2009 after exclusion of damaged/obsolete stock is made, there will not be any difference in the valuation of stock.

4. The Ld. DR on the other hand heavily placed his reliance on the order of authorities below.

5. We have heard the rival parties and have gone through the material placed on record. We find that as regards the disallowance u/s 40A(3), the assessee had made payments exceeding Rs.20,000/- on three occasions on 26.04.2008, 12.05.2008 and 14.07.2008 and the violation

is only on account of nominal increase against the amount of Rs.20,000/-. We further find that these payments had been made to the truck drivers who generally insist on cash payments. The Assessing Officer has not doubted the genuineness of these payments and has disallowed the amount holding that assessee was bound to make the payments through Banking Channels. However, we find that where the genuineness of payments is not doubted the disallowance u/s 40A(3) should not be made. The Central Board of Direct Taxes vide Circular No. 220 dated 31.05.1977 has clarified that no disallowance u/s 40A(3) of the I. T. Act shall be made where the assessee satisfies the ITO that the payment could not be made by way of a crossed cheque drawn on a bank or by a crossed bank draft due to certain exceptional circumstances. The Amritsar Bench in the case of Sh. Atul Gupta in ITA No. 465/Asr/2016 vide order dated 24.08.2017 has decided the issue regarding violations u/s 40A(3) in favour of assessee by holding as under:

“11. The Central Board of Direct Taxes vide Circular No. 220 dated 31.05.1977 has issued instructions regarding disallowance u/s 40A(3) read with rule 6DD(j) of the IT Rules, and wherein the Board has clarified that no disallowance u/s 40A(3) of the I.T. Act shall be made where the assessee satisfies the ITO that the payment could not be made by way of a crossed cheque drawn on a bank or by a crossed bank draft due to certain exceptional circumstances. In the circular the Board has also given certain illustrations and has further stated that the said illustrations are only illustrative not exhaustive and there could be other circumstances also.

12. In the present case, the assessee is working from an area in Rajouri which undisputedly is a disturbed area. Moreover cash payments has been certified by payee to have been received by it. The Assessing Officer had no doubt about the genuineness of these transactions. Cash transaction constituted only about 15% of the total payments. Under these

circumstances it can safely be said that such cash payments were made under exceptional and unavoidable circumstances. In view of the disturbed conditions due to terrorism no one would like to keep cash with himself and therefore it is prudent on the part of any person to hand over the cash to supplier instead of keeping with himself. The Hon'ble Supreme Court in the case of Attar Singh Gurmukh Singh Vs. ITO 191 ITR 667 while dealing with the violation of provisions of section 40A(3) has held as under:

“In our opinion, there is little merit in this contention. Sec. 40A(3) must not be read in isolation or to the exclusion of r. 6DD. The section must be read along with the rule. If read together, it will be clear that the provisions are not intended to restrict the business activities. There is no restriction on the assessee in his trading activities. Sec. 40A(3) only empowers the Assessing Officer to disallow the deduction claimed as expenditure in respect of which payment is not made by crossed cheque or crossed bank draft. The payment by crossed cheque or crossed bank draft is insisted on to enable the assessing authority to ascertain whether the payment was genuine or whether it was out of the income from undisclosed sources. The terms of s. 40A(3) are not absolute. Considerations of business expediency and other relevant factors are not excluded. Genuine and bona fide transactions are not taken out of the sweep of the section. It is open to the assessee to furnish to the satisfaction of the Assessing Officer the circumstances under which the payment in the manner prescribed in s. 40A(3) was not practicable or would have caused genuine difficulty to the payee. It is also open to the assessee to identify the person who has received the cash payment. Rule 6DD provides that an assessee can be exempted from the requirement of payment by a crossed cheque or crossed bank draft in the circumstances specified under the rule. It will be clear from the provisions of s. 40A(3) and r. 6DD that they are intended to regulate business transactions and to prevent the use of unaccounted money or reduce the chances to use black money for business transactions. [See Mudiam Oil Co. vs. ITO (1973) 92 ITR 519 (AP) : TC18R.450]. If the payment is made by a crossed cheque drawn on a bank or a crossed bank draft, then it will be easier to ascertain, when deduction is claimed, whether the payment was genuine and whether it was out of the income from disclosed sources. In interpreting a taxing statute, the Court cannot be oblivious of the proliferation of black money which is under circulation in our country. Any restraint intended to curb the chances and opportunities to use or create black money should not be regarded as curtailing freedom of trade or business.”

The Hon'ble Delhi High Court in the case of R. C. Goel Vs. Commissioner of Income Tax has also considered the application of provisions of u/s 40A(3) under exceptional circumstances and has allowed the appeal of assessee by holding as under:-

“In the present case, the assessee in terms of its contract is bound to maintain constant supplies in the trains and ensure that at no

point in time can the passengers be deprived of these articles. In the course of such transactions, it sources these articles from M/s Shruti Enterprises, Mumbai based concern. Apparently, that concern is also a small time one and insists on cash payments for ensuring continuity and timely supplies. Whilst, the Court is conscious and does not in any manner wish to comment' adversely on the larger public interest element embedded in Section 40A and the underlying principle, at the same time, the Court also notes that the proviso seeks to relieve to a certain extent, the measure of hardship which might be imposed upon small businesses and professionals who are engaged in activities and are dependent entirely on timely cash flow. It is in such cases that Rule 6DD - which was formulated as a proviso to Section 40A (3) - steps in to aid such assesseees and concerns. In this context, the statutory mandate in Section 6DD (k), at least in the circumstances of the case, has to be so construed as to mean that bur for the cash payment, the assessee would have been deprived the benefit of supplies itself. This Court clarifies that the interpretation of the expression "who is required to make payment in cash" having regard to the circumstances of the case is fact dependent, at least in the present case. The consequence of instances of payment through account payee cheques in small business which are dependent on such supplies would be to completely stifle, if not stop, the business activities. It is in that sense that the expression "required" would have to be construed."

In the other case laws relied on by the assessee including the decisions of Amritsar Bench in the case of Sh. Rakesh Kumar Vs. ACIT, Circle02, Bathinda. The Amritsar Bench while allowing the appeal of assessee has also followed the decision of Hon'ble Supreme Court in the case of Attar Singh Gurmukh Singh Vs. ITO (supra).

The relevant part of the order of Amritsar Bench in the case of Sh. Rakesh Kumar Vs. ACIT Circle-II Bathinda, is reproduced below:-

"14. About this clause, many doubts were raised and enquiries were directed to the Board as to what shall constitute exceptional and unavoidable circumstances within the meaning of Clause (j). That led to issuance of Circular by the Board on May 31, 1977 ([1977] 108 ITR (St.) 8), which is published in Taxmann, Vol. 1, 1988 Edition. Significantly paragraph 4 of the aforesaid Circular ous very clearly that all the circumstances in which the conditions laid down in Rule 6DD(j) could be applicable cannot be spelt out. However, some of them which will seem to meet the requirements of the said rule are as follows:

- 1. the purchaser is new to the seller; or*
- 2. the transactions are made at a place whether either the purchaser or the seller does not have a bank account; or*
- 3. the transactions and payments are made on a bank holiday;*
or

4. *the seller is refusing to accept the payment by way of crossed cheque/draft and the purchaser's business interest would suffer due to non-availability of goods otherwise than from this particular seller ; or*
5. *the seller, acting as a commission agent, is required to pay cash in turn to persons from whom he has purchase the goods; or*
6. *specific discount is given by the seller for payment to be made by way of cash.*

15. *It was further clarified in paragraph 6 that the above circumstances are not exhaustive but illustrative.*

16. *.Therefore, in our opinion, the Tribunal was clearly in error in not traveling beyond the circumstances referred to in paragraph 4 of the Circular and to consider the explanation submitted by the assessee on its own merit.*

17. *Significantly paragraph 5 reproduced herein below gives a clear indication that Rule 6DD(j) has to be liberally construed and ordinarily where the genuineness of the transaction and the payment and identity of the receiver is established, the requirement of Rule 6DD(i) must be deemed to have been satisfied. Paragraph 5 of the Circular reads as under [1977] 108 ITR (St.) 8, 9:*

5. It can be said that it would, generally, satisfy the requirements of Rule 6DD(j), if a letter to the above effect is produced in respect of each transaction falling within the categories listed above from the seller giving full particulars of his address, sales tax number/permanent account number, if any, for the purposes of proper identification to enable the Income-tax Officer to satisfy himself about the genuineness of the transaction. The Income-tax Officer will, however, record his satisfaction before allowing the benefit of Rule 6DD(j).

18. *It appears that fulfillment of the conditions of paragraph 5 of the circular has clearly escaped the attention of the Tribunal. The circular clearly indicates that ordinarily where the Income-tax Officer is satisfied about the genuineness of the transaction and payment and identification of the cash payment is established, the Income-tax Officer shall record his satisfaction about the fulfillment of the conditions for allowing the benefit of Rule 6DD(j). Apparently, Section 40A(3) was intended to penalize the tax evader and not the honest transactions and that is why after framing of Rule 6DD (j), the Board stepped in by issuing the aforesaid circular.*

19. *This clarification, in our opinion, is in conformity with the principle enunciated by the Supreme Court in CTO v. Swastik Roadways as noticed above.*

20. *In this case, there is no dispute about the genuineness of the transactions and the payment and identity of the receiver are established. Therefore, the case clearly fell within the parameters of paragraphs 4 and 5 of the aforesaid circular read together."*

8. *The respondent's case is also supported by the judgment of the Supreme Court in Attar Singh Gurmukh Singh v. ISO [1991] 191 ITR 667/59 Taxman 11. After referring to Rule 6DD, the Supreme Court held:-*

"7. In our opinion, there is little merit in this contention. Section 40-A(3) must not be read in isolation or to the exclusion of Rule 6-DD. The section must be read along with the rule. If read together, it will be clear that the provisions are not intended to restrict the business activities. There is no restriction on the assessee in his trading activities. Section 40-A (3) only empowers the assessing officer to disallow the deduction claimed as expenditure in respect of which payment is not made by crossed cheque or crossed bank draft. The payment by crossed cheque or crossed bank draft is insisted on to enable the assessing authority to ascertain whether the payment was genuine or whether it was out of the income from disclosed sources. The terms of Section 40-A(3) are not absolute. Consideration of business expediency and other relevant factors are not excluded. The genuine and bona fide transactions are not taken out of the sweep of the section. It is open to the assessee to furnish to the satisfaction of the assessing officer the circumstances under which the payment in the manner prescribed in Section 40-A(3) was not practicable or would have caused genuine difficulty to the payee. It is also open to the assessee to identify the person who has received the cash payment. Rule 6-DD provides that an assessee can be exempted from the requirement of payment by a crossed cheque or crossed bank draft in the circumstances specified under the rule. It will be clear from the provisions of Section 40-A(3) and Rule 6-DD that they are intended to regulate the business transactions and to prevent the use of unaccounted money or reduce the chances to use black money for business transactions. [See: Muddiam Oil Company v. ITO [(1973) 92 ITR 519 (API)]. If the payment is made by a crossed cheque drawn on a bank or a crossed bank draft then it will be easier to ascertain, when deduction is claimed, whether the payment was genuine and whether it was out of the income from disclosed sources. In interpreting a taxing statute the court cannot be oblivious of the proliferation of black money which is under circulation in our country. Any restraint intended to curb the chances and opportunities to use or create black money should not be regarded as curtailing the freedom of trade or business."

9. *At the cost of repetition, the Tribunal has not disbelieved the transactions or the genuineness thereof. Nor has it disbelieved the fact of payments having been made. More important, the reasons furnished by the appellant for having made the cash payments, which we have already adverted to, have not been disbelieved. In our view, assuming these reasons to be correct, they clearly make out a case of business expediency.*

10. *In the circumstances, the order of the Tribunal in this regard is set aside. The payments cannot be disallowed under Section 40A(3) of the Act."*

9. *In view of the above, facts and circumstances and in view of the judicial precedents, we do not find any infirmity in the order of Ld. CIT(A). Therefore, the appeal filed by Revenue is dismissed.”*

In view of the above, keeping in view the exceptional circumstances and in view of the amount involved, we delete the disallowances u/s 40A(3) sustained by Ld. CIT(A).

As regards the valuation of the stock at the time of survey, we find that the break up of stock found included an amount of Rs.12750/- which is on account of empty drums and which the assessee had claimed at the time of survey itself that these do not belong to it and these are to be returned. This fact is verifiable from P.B. page 34 where the details of drums mentioned as returnable is placed, therefore the addition of Rs.12750/- is not justified as this item of stock did not belong to the assessee.

As regards the addition on account of consumable stock amount to Rs.111740/- as per the details as P.B. 35, we find that the amount of consumable stores were actually lying at the premises and which the assessee had not declared in the stock statement. Therefore the addition is justified as the assessee was bound to pass entry in the profit and loss account relating to expenses of consumable stores after reducing the closing stock left over on account of consumable stores and therefore this grievance is not justified and we uphold the action of Ld. CIT(A) as regards addition on account of valuation of consumable stores.

As regards the difference in valuation of finished goods as placed at P.B. page 25, we find that at the time of survey the ply relating to sizes 4 mm and 3 mm were valued at the rate of Rs. 51.66 per sq. m. whereas the cost of the plies measuring 4 mm and 3mm as per stock statement as on 31.03.2009 was Rs. 40 and 45 respectively. The valuation of stock as on 31.03.2009 has not been doubted by the Assessing Officer and therefore the Assessing Officer should have applied this rate for arriving at the value on account of these plies specifically in view of the fact that assessee had explained the difference to Assessing Officer vide undated letter placed at P.B. 1, 2 and 3. The assessee vide this letter had explained the total difference in respect of various sizes and the authorities below should have considered the same. We further find that the closing stock found at the time of survey included damaged/cut pieces and obsolete stock. This fact is verifiable from the inventory of stock itself placed at P.B. page 25 where the obsolete stocks/damaged stocks falling in the category of 4mm/3mm, 12mm/9mm and 18mm has been mentioned by adding separately on lump sum basis the quantity of 2000 sq. ft., 500 sq. ft., 1000 sq. ft. and 500 sq. ft. under various categories. The assessee had explained these facts vide letter addressed to Assessing Officer placed at P.B. page 1 to 3. The Assessing Officer in his order has noted down these contentions. The Assessing Officer has also noted down the contentions of assessee that there was difference in valuation of stock as the same has to be valued on cost price basis but still he did not verify the claim of assessee and made the additions. In

this respect the contentions of assessee as noted by Assessing Officer are quite relevant which for the sake of completeness are reproduced below:

“(C). The valuation of ply, board, finished stock for the valuation of finished goods it has been observed that ply cut pieces / damage pieces of 4000 sq.m have been valued at the billing price. The 4000 sq. m damaged ply cannot be valued at the selling price as it does not fetch any amount and is lying for the past 4 to 5 years. If we reduce the sale price of 4000 sq.m. @ 51.66, Rs 135 and Rs 55.00. The difference will reduce by Rs 300820/-. Further they have also applied the average rate 51.66 to 4mm PF and 3mm Comm which comes to Rs 2,21,414/- by actually multiplying the quantity with the assessable value the amount comes to Rs 2,26,175/-. There is app. no difference in the amount calculated by us. 12mm, 9mm & 12mm PF the valuation team has calculated value at Rs 9,84,420/- where as per actual calculation it comes to Rs 7,04,047/- so the difference of Rs 2,12,783/- exists which has been over valued by the survey team. In 18mm the stock has been as 515 sq. m and after excluding 500 on account of defective / damage. The sq. m comes to 15 sq. m and by applying the rate of 140 it comes to Rs.2,250/- only so there is no difference on his account. The total difference of Rs.111740/- 12750/- 300820/-, 212873/- comes to Rs.6,33,423/-“

In view of the above facts and circumstances we delete the additions in the valuation of stock consisting of following items:

Obsolete/damaged stock	Rs.3,00820=00
Over valuation of stock	Rs.212873=00
Valuation of Drums	Rs.12750=00
Total	Rs.5,26,443=00

The amount of deletion out of addition in stock is almost equal to the addition of Rs.527503/- and the difference is insignificant and therefore we delete the whole of addition on account of difference in stock.

7. In view of the above, the appeal filed by assessee is allowed.

Order pronounced in the open court on 04.12.2017

Sd/-
(N. K. CHOUDHRY)
JUDICIAL MEMBER

Sd/-
(T. S. KAPOOR)
ACCOUNTANT MEMBER

Dated: 04.12.2017.

/GP/Sr. Ps.

Copy of the order forwarded to:

- (1) The Assessee:
- (2) The
- (3) The CIT(A),
- (4) The CIT,
- (5) The SR DR, I.T.A.T.,

True copy

By Order