

आयकर अपीलीय अधिकरण, अहमदाबाद न्यायपीठ 'B' अहमदाबाद ।

IN THE INCOME TAX APPELLATE TRIBUNAL

“B” BENCH, AHMEDABAD

**BEFORE SHRI PRADIP KUMAR KEDIA, ACCOUNTANT MEMBER
& SHRI MAHAVIR PRASAD, JUDICIAL MEMEBR**

आयकर अपील सं./I.T.A. No. 2193/Ahd/2014

(निर्धारण वर्ष / Assessment Year : 2010-11)

The Asstt. Commissioner of Income-tax, Kheda Circle, Nadiad	बनाम/ Vs.	M/s. Dattatray Poultry Breeding Farm Pvt. Ltd., At. & Po. Surasamal, Ta: Nadiad, Dist. Kheda- 387115
स्थायी लेखा सं./जीआइआर सं./PAN/GIR No. : AAACD8192M		
(अपीलार्थी /Appellant)	..	(प्रत्यर्थी / Respondent)

अपीलार्थी ओर से /Appellant by :	Shri Mudit Nagpal, Sr.D.R.
प्रत्यर्थी की ओर से / Respondent by :	Shri Jaimin Gandhi, A.R.

सुनवाई की तारीख / Date of Hearing	06/06/2018
घोषणा की तारीख /Date of Pronouncement	19/06/2018

आदेश/ORDER

PER PRADIP KUMAR KEDIA - AM:

The captioned appeal has been filed at the instance of the Revenue against the order of the CIT(A)-IV, Baroda ('CIT(A)' in short), dated 20.05.2014 arising in the assessment order dated 12.03.2013 passed by the Assessing Officer (AO) u/s.143(3) of the Income Tax Act, 1961; (the Act) concerning assessment year 2010-11.

2. The grounds of appeal raised by the Revenue reads as under:

“1. On the facts of the case and in the circumstances and in law, the CIT(A)-IV, Baroda has erred in deleting the addition of Rs.72,49,188 made by the AO u/s.41(1) of the I.T. Act, in respect of the cessation of liability ignoring the fact that the purported creditors shown as outstanding in the books for several years were unsupported by complete addresses and were non-traceable and the assessee on few instances did not dispute about closure of its account in rival party's books.

2. On the facts of the case and in the circumstances and in law, the CIT(A)-IV, Baroda has erred in deleting the addition of Rs.72,49,188 made by the AO running over the eyes on Explanation 1 below section 41(1) conspicuously spells out that loss or expenditure or some benefit in respect of any such trading liability by way of remission or cessation thereof shall include the remission or cessation of any liability and this rudimentary principle gets support from the decision in the case of CIT v/s Chipsoft Technology (P.) Ltd. reported in 26 taxmann.com 109 [Delhi].

3. On the facts of the case and in the circumstances and in law, the CIT(A)-IV, Baroda has erred in deleting addition of Rs.72,49,188 made by the AO ignoring the factum that section 41(1) is a deeming provision and legal disability is applicable even in the absence of unilateral act of remission or cessation of any liability by the assessee as per principles of Law of limitation.”

3. Briefly stated, the assessee, a domestic company, is engaged in the business of job work of hatching of eggs for Saguna Poultry Farm Ltd., Chennai. In the course of scrutiny assessment, the AO observed from the balance sheet filed by the assessee that assessee has shown sundry creditors outstanding for payment by the assessee at Rs.74,40,360/-. In order to ascertain the bonafides of the sundry creditors reflected in the balance sheet. The AO made inquiries with certain creditors under s.133(6) of the Act. It was found by the AO that certain creditors have categorically denied that they have not made any transaction with the assessee. It was also simultaneously observed that notices in some cases have returned unserved by the postal authority and the assessee failed to produce the said creditors as directed. The AO also *inter alia* noted that the assessee has not

even furnished the correct address of all the creditors, PAN numbers and confirmation in respect of the creditors. In the light of these facts, the AO also doubted the bonafides of the creditors. The AO also observed the claim of the assessee that outstanding is on account of purchases made does not appear plausible considering the nature of business carried out by the assessee. It was observed that the assessee is only doing job work and hence, there is no possibility of the purchases from the creditors is claimed. It was found that the creditors are standing in the books for last many years without payment. It was further observed that the assessee has not furnished any corroborative evidences regarding purchases made from the creditors. The AO therefore came to the conclusion that in the light of these peculiar facts where the creditors are outstanding for long period and the parties are not traceable, denied transactions and not demand money etc. the genuineness of the creditors remains unproved and the onus cast upon the assessee in this regard has not been discharged. However, the AO accepted bonafides in the case of two creditors where the corroboration was available. Consequently, the AO held that Rs.72,49,188/- out of Rs.74,40,360/- shown as creditors' liability are not genuine and treated the same as cessation of liability within the meaning of Section 41(1) of the Act and added the same to the total income of the assessee. The aforesaid action of the AO was challenged by the assessee before the CIT(A).

4. The CIT(A) revisited the submissions made on behalf of the assessee in this regard and also referred to certain judicial pronouncements and found merit in the appeal of the assessee. It will be apt to reproduce the relevant operative para of the order of the CIT(A) dealing with the issue:

“4.2 I have considered the appellant's submissions and the Assessing Officer's observations. In this case, the appellant had not been able to give the addresses of many sundry creditors. Besides, in some cases in which addresses were available the notice u/s. 133(6) could not be served at those addresses. In 5 cases, other parties did not confirm that they had to receive some amount from the appellant. But it is also a fact that there was no transaction with these sundry creditors during the F.Y. 2009-10. Besides, the appellant has not written off these amounts in its books of accounts. On similar facts, the Hon'ble Gujarat High Court in its decision in the case of Bogilal Ramajbhai Atara (Supra) has held after discussing the discussions in the case of Miraa Processors Pvt. Ltd 208 taxmann.com 93 (Guj), Nitin S. Garg, 208 taxmann.com 16 (Guj) and G.K. Patel & Company 2012 taxmann.com 384 (Guj) as follows:

'We are in agreement with the view of the Tribunal. Section 41(1) of the Act as discussed in the above three decisions would apply in a case where there has been remission or cessation of liability during the year under consideration subject to the conditions contained in the statute being fulfilled. Additionally, such cessation or remission has to be during the previous year relevant to the assessment year under consideration. In the present case, both elements are missing. There was nothing on record to suggest there was remission or cessation of liability that too during the previous year relevant to the assessment year 2007-08 which was the year under consideration. It is undoubtedly a curious case. Even the liability itself seems under serious doubt. The Assessing Officer undertook the exercise to verify the records of the so called creditors. Many of them were not found at all in the given address. Some of them, were not found at all in the given address. Some of them stated that they had no dealing with the assessee. In one or two cases, the response was that they had no dealing with the assessee nor did they know him. Of course, these inquiries were made ex parte 'and in that view of the matter, the assessee would be allowed to contest such findings. Nevertheless, even if such facts were established through bi-parte inquiries, the liability as it stands perhaps holds that there was no cessation or remission of liability and that therefore, the amount in question cannot be added back as a deemed income under section 41 (c) of the Act. This is one of the strange cases where even if the debt itself is found to be non-genuine from the very inception, at least in terms of section 41(1) of the Act there is no cure for it Be that as it may, insofar as the orders of the Revenue authorities are concerned, the Tribunal not having made "any error, this Tax Appeal is dismissed."

4.2.1. Thus, the issue in this case is covered squarely in favour of the appellant by the decisions of Hon'ble Gujarat High Court discussed above. Hence, following the same, Assessing Officer is directed to delete the addition made by him u/s. 41(1) of the Act."

5. In essence, the CIT(A) observed that where the assessee has not written back these amounts as income in its books of accounts such outstanding liabilities cannot be regarded as income under s. 41(1) of the Act. The CIT(A) also relied upon the decision of the hon'ble Gujarat High Court in the case of Bhogilal Ramjibhai Atara 227 Taxman 313(Guj) and concluded that Section 41(1) of the Act has no application in the facts of the case. He accordingly exonerated the assessee from the clutches of Section 41(1) of the Act and reversed the action of the AO in this regard.

6. Aggrieved by the aforesaid action of the CIT(A), the Revenue is in appeal before the Tribunal.

7. Learned DR for the Revenue submitted at the outset that existence of liability shown in the balance sheet is under serious doubt. The AO has undertaken detailed verification of the factual aspects and found that the facts of the case are gross and peculiar. It is a matter of record that creditors were either not traceable or have actually denied the existence of these long outstanding liability. In such a factual matrix, the CIT(A) has misdirected himself in law and on facts in summarily adjudicating the issue in favour of the assessee. As regards the reliance placed by the CIT(A) on the decision of the hon'ble Gujarat High Court in the case of CIT vs. Bhogilal Ramjibhai Atara (supra), the learned DR submitted that the law has evolved over a period of time since the decision of the aforesaid hon'ble Gujarat High Court. The learned DR made reference to the recent decision of the hon'ble Gujarat High Court in the case of Gujtron Electronics (P.)

Ltd. vs. ITO (2017) 83 taxmann.com 389 (Guj) and contended that the hon'ble Gujarat High Court in the later decision has clearly held that cessation of liability occurred where not a single customer had demanded money back nor assessee had made any attempt to repay the same. It was also observed by the hon'ble Gujarat High Court that in such a situation where the liability is reflected in the books of accounts whereas over years, assessee had also invested such amount and earned interest and used such interest for its purpose, the AO was justified in adding the impugned amount to the income of the assessee on the grounds of cessation of liability contemplated u/s.41(1) of the Act. It was also pointed out that the hon'ble Gujarat High Court took cognizance of the fact that there is absolutely no movement or correspondence between assessee and its creditors with respect to the claim or with respect to the deposited amounts while deciding the issue against the assessee. The learned DR thereafter referred to another judgment rendered by the hon'ble Delhi High Court in the case of CIT vs. Chipsoft Technology (P.) Ltd. (2012) 210 Taxman 173 (Delhi) to buttress its plea that Explanation to Section 41(1) does not restrict the scope of Section 41(1) only to a situation where the assessee writes back the liability in its books of accounts as per its option. The learned DR in conclusion submitted that where as a matter of fact it is found that existence of the creditors claimed in the books of accounts is found to be incorrect or in-genuine, the operation of Section 41(1) to assess the non-existent trade liability by resorting to Section 41(1) cannot be excluded.

8. The learned AR, on the other hand, strongly supported the order of the CIT(A) and submitted that the provisions of Section 41(1) can apply only where; (i) there is a positive act on the part of the assessee for writing back the liabilities as income in the P&L account, (ii) the

liability ceases to exist by the reason of operation of law i.e. on the liability becoming unenforceable at law, (iii) by discharge of the debt as referred to in the decision of the Hon'ble Supreme Court of India in CIT vs. Sugauli Sugar Works (P.) Ltd. 236 ITR 518 (SC). The learned AR insisted that merely because the liabilities have remained outstanding in the books of accounts for last many years is an irrelevant consideration to ascertain taxability with reference to Section 41(1) of the Act. It was also contended that the expiry of period of limitation prescribed under the Limitation Act cannot extinguish the debts as it would only prevent the creditor from enforcing these debts. The learned AR submitted that in the absence of removal of the liability from the balance sheet by way of write back, no benefit can be said to be conferred on the assessee by way of cessation which can be deemed to be profit and gains of business of the assessee. The learned AR next referred to the decision of hon'ble Gujarat High Court in the case of CIT vs. Bhogilal Ramjibhai Atara (supra) and submitted that in that case also, the AO undertook exercise to verify the records of the so called creditors and found that creditors had no dealing with the assessee. It was further found by the AO therein that debts were outstanding since last several years. In the backdrop of these facts where some of the parties were not found at the given address or some of the parties have stated that they had no concern with the assessee; some of the parties conveyed that they did not even know the assessee and thus where the liability itself found to be in serious doubt, the hon'ble Gujarat High Court held that no cure is available to the Revenue in terms of Section 41(1) of the Act. Learned AR restated in elaboration that Section 41(1) would apply only in a case where there has been remission or cessation of liability during the year under consideration subject to the conditions to be fulfilled as stated in the provision. Besides, the learned AR contended

that the AO has not brought any evidence on record to establish that such cessation or remission has taken place during the previous year relevant to assessment year under consideration. This apart, the learned AR next contended that Section 41(1) of the Act comes into play only where the liability do exists earlier which ceases to exist during the financial year under consideration. Therefore, Section 41(1) presupposes existence of liability in the earlier year. The learned AR accordingly submitted that scope of Section 41(1) requires to be read in distinction to Section 68 of the Act. Adverting to the decision of the hon'ble Gujarat High Court in the case of Gujtron Electronics (supra) relied upon by the other side, the learned AR contended that the aforesaid decision was rendered in the backdrop of altogether different facts. It was submitted that in Gujtron Electronics's case (supra), the liability was nearly 15 to 20 years back in relation to sales promotion scheme when the company was engaged in the manufacturing of goods. The company thereafter was no longer engaged in such manufacturing activity and was now engaged only in trading of electronics appliances etc. The learned AR submitted that, notably, scheme itself suggested that it was valid for a period of twelve months. Since years, there was no activity and since the scheme itself was dispensed, the liability had actually ceased to exist. The learned AR thus submitted that cessation of liability had occurred as a matter of fact. The learned AR thus submitted that in view of the material difference in the facts, the decision in Gujtron Electronics's case (supra) has no application to the facts of a case. The learned AR thus submitted that the CIT(A) has decided the issue in right perspective and no interference thereof is called for.

9. We have carefully considered the rival submissions and perused the orders of the authorities below and the case laws cited at bar. The

applicability of Section 41(1) of the Act on outstanding trading liabilities as reflected in the balance sheet has been called into question. Section 41(1) of the Act states that where an allowance in respect of an expenditure or trading liability etc. is made in a year and the assessee obtains any benefit, whether in cash or otherwise in a subsequent year, such benefit shall be deemed to be profits & gains of the business of that subsequent year, whether such business is in existence or not in that subsequent year. The Section has an effect of deeming such cessation or remission of liability as income in departure with the general law where such remission or cessation is not regarded as an income. Coming to the facts, as noted above, it is the case of the Revenue that the trading liabilities of Rs.74.40 Lakhs claimed to be payable to several parties was not found to be subsisting liability as per the outcome of inquiries made in this regard. The AO noted on facts that the creditors shown in the books are for purchase of goods whereas the assessee is engaged in job work and therefore outstanding towards purchase of goods is a high suspect. The AO based on inquiry; observed that many of the creditors could not be traced on the address given by the assessee. Many others have denied making any transaction with the assessee. Coupled with this, such huge amounts of outstanding remains in the books for last six to twenty years without any repayment. On these facts, the AO concluded that liability shown in the balance sheet to be a non-existing liability and accordingly invoked Section 41(1) of the Act for the purposes of taxability of such non-existent liability as chargeable income of the assessee owing to the fact that the assessee has obtained benefit in the past against such outstanding trading liabilities. The CIT(A), in first appeal, however, has set aside the action of the AO primarily on the ground that the assessee has not written back of these amounts in the books of accounts. The CIT(A) granted relief to the

assessee placing reliance upon the decision of the hon'ble Gujarat High Court in its decision in the case of Bhogilal Ramjibhai Atara (Supra).

10. It is the case of the Revenue that the law has evolved judicial precedents since the earlier decision of the hon'ble Gujarat High Court in the case of Bhogilal Ramjibhai Atara's case (supra). Keeping in mind the peculiar facts as found by the AO, we observe that hon'ble Gujarat High Court was confronted with the similar issue in the case of Gujtron Electronics's case (supra) where also the facts are broadly similar. In Gujtron Electronics's case (supra) also the outstanding was appearing in the balance sheet during the year under consideration and was not actually written off by the Assessee. However, the hon'ble Gujarat High Court noted that not a single customer had demanded money back nor assessee had made any attempt to repay the same. Over year, company had invested such amount in diverse activities. On such facts where since last many years, there was no activity of any repayment of amounts nor the amounts have been collected by the customers, the hon'ble Court endorsed the decision of the co-ordinate bench of tribunal (ITA No.1145/Ahd/2016 order dated 10.01.2017) that trading liability had, in fact, ceased to exist. Therefore, it logically flows that the hon'ble Gujarat High Court has clearly opined that liability may cease to exist in terms of Section 41(1) where it is outstanding for a long period without any payment despite it being reflected in the books of accounts. The hon'ble Gujarat High Court also did not question the action of Revenue towards taxability u/s.41(1) of the Act with reference to financial year in question. The distinction sought to drawn on behalf of Assessee for its non-application is un-merited. The Hon'ble Gujarat High Court has approved the findings of ITAT that Section 41(1) of the Act would apply where liabilities outstanding are found to be not payable for one

or more reasons. We notice that similar views have been echoed by the hon'ble Delhi High Court in the case of CIT vs. Chipsoft Technology (supra) cited on behalf of Revenue. The hon'ble Delhi High Court in that case observed that the assessee could not claim benefit of showing unpaid dues of employees outstanding for 6-7 years and it was found that there was cessation of such liability on facts which was liable to be added to the income of the assessee. The hon'ble Delhi High Court also negated the contention of assessee that a liability does not cease as long as it is reflected in the books and that mere lapse of time given to the creditor to recover the amount due does not efface the liability. The hon'ble High Court took note of expression 'include' occurring in Explanation to Section 41(1) of the Act and held that the Explanation does not restrict the scope of remission or cessation of any liability by a unilateral act alone. The hon'ble High Court held that in view of the phraseology of Explanation to Section 41(1), even omission to pay over a period of time and resultant benefit derived by the assessee would qualify as cessation of liability *albeit* by operation of law. In this backdrop, where the Revenue Authorities have found as a matter of fact after detailed inquiry that the liabilities shown in the balance sheet do not, in fact, exist, the Revenue Authorities are not expected to put blinkers while looking at the outstanding trading liability. Merely because the liabilities have been shown in the books of accounts and not written back, would not, in our view tie down the Revenue to hold such liabilities to be subsisting liability. The ground realities on facts were found to be altogether different in the present case. It does not accord with human probabilities to infer that trading liabilities do exist where the parties are not traceable, denied the outstanding, no repayment made for last many many years and till date. Such approach would be quite theoretical and abstract.

11. Adverting to the legal claim made before us on behalf of the assessee that liabilities shown in the balance sheet was itself sufficient to hold such liability exists and bonafide is not understood at all. The liabilities shown in the balance sheet as existing by assessee was found to be symbolic by AO. The onus is on the assessee to show the reasons why it believed at the time of filing the return that the liabilities were true. No such attempt was even made to prove the existence of liabilities. In this view of the matter, the incidence of taxation under s.41(1) of the Act cannot be escaped on non-existing liability. Our this view also finds support from yet another decision of the hon'ble Bombay High Court in the case of Palkhi Investments and Trading Co. Pvt. Ltd. vs. ITO 288 CTR 473 (Bom.) where the hon'ble Bombay High Court went to the extent of confirming penalty for not offering such trading liability under s.41(1) of the Act. Thus, the conclusion apparently leans against the Assessee. However, we are left with one pertinent question hurled at us on behalf of the Assessee i.e. year of taxability. In this regard, we are not impressed by the plea the AO did not bring anything on record to allege that cessation took place during the financial year in question for the purposes of taxability under s.41(1) of the Act. We find that AO has assertive justification to bring the outstanding liability within the net of s.41(1) of the Act in the Financial Year under inquiry. The onus is on the Assessee to show that year of cessation is different. In the instant case, the Assessee does not admit cessation at first place. The AO therefore is within its right to hold the Financial Year in question as the right year for taxability when the facts concurring the non-existence were unrevealed. The Assessee was failed to discharge onus. Besides, the defect of year of taxation if any can be cured under s.153(6) in such cases. However, we do not consider it expedient to dwell further. In the totality of the facts and

circumstances, we find ourselves in agreement with the view taken by the AO that addition made in respect of trading liabilities which had ceased to exist represents taxable business income in terms of Section 41(1) of the Act. The CIT(A) in our view has committed error in disregarding the gross facts unearthed in the present case while deciding in favour of the assessee. The order of the CIT(A) is therefore set aside and the order of the AO on the issue is restored.

12. In the result, the appeal of the Revenue is allowed.

This Order pronounced in Open Court on 19/06/2018
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Sd/-
(MAHAVIR PRASAD)
JUDICIAL MEMBER

Ahmedabad: Dated 19/06/2018

Sd/-
(PRADIP KUMAR KEDIA)
ACCOUNTANT MEMBER

True Copy

S. K. SINHA

आदेश की प्रतिलिपि अद्योषित / Copy of Order Forwarded to:-

1. राजस्व / Revenue
2. आवेदक / Assessee
3. संबंधित आयकर आयुक्त / Concerned CIT
4. आयकर आयुक्त- अपील / CIT (A)
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, अहमदाबाद /
DR, ITAT, Ahmedabad
6. गार्ड फाइल / Guard file.

By order/आदेश से,

उप/सहायक पंजीकार
आयकर अपीलीय अधिकरण, अहमदाबाद ।