

IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED: 27.04.2012

CORAM:

THE HONOURABLE MRS.JUSTICE CHITRA VENKATARAMAN
and
THE HONOURABLE MR.JUSTICE K.RAVICHANDRA BAABU

Tax Case (Appeal) No.1113 of 2005

M/s.Tarapore & Co.
Dhun Building, 827, Anna Salai
Chennai-600 002. .. Appellant

versus

The Deputy Commissioner of Income Tax
Special Range IX
Chennai-600 034. .. Respondent

PRAYER: Tax Case Appeal filed under Section 260A of the Income Tax Act, 1961, against the order of the Tribunal dated 26.07.2005 made in I.T.A.No.1666 of 1997 on the file of the Income Tax Appellate Tribunal Chennai 'B' Bench.

For appellant : Mr.V.S.Jayakumar

For respondent : Mr.T.S.Senthil Kumar
Standing Counsel for Income Tax

JUDGMENT

(Judgment of the Court was delivered by CHITRA VENKATARAMAN,J.)

The following are the substantial questions of law raised by the assessee on which this Tax Case Appeal was admitted by this Court:

1. Whether the Tribunal was right in law in holding that the sum of Rs.55,72,981/- is to be treated as income even though the assessee has disclosed the value of goods as part of closing stock?
2. Whether the Tribunal is right in law in ignoring that the role of the assessee with regard to the goods supplied by supplier is only that of a bailee and so the value of goods cannot constitute income in its hands?

2. Learned counsel appearing for the assessee submits that he is not pressing the second substantial question of law. An endorsement to that effect has also been made by the learned counsel appearing for the assessee. Hence, the question that survives for consideration herein is the first substantial question of law.

3. The assessment year under consideration is 1987-88. The assessee herein had an agreement with Naval Science and Technological Laboratory (NSTL) for the execution of work under an agreement dated 22nd August 1985. The agreement related to civil works of High Speed Towing Tank Complex. The contract execution contemplated that the assessee herein, as a contractor, shall provide all materials including steel and cement, labour, energy and water, all tools, tackles, plant and transport, necessary for the proper execution of the work to the satisfaction of the owner, namely NSTL. The total contract price as per the contract was given as Rs.5,07,55,102/-. Article 4 gives the details of the contract price, which is stated to have been arrived at based on the quantities and the rates as stated in Annexure IV of the agreement. Article 4.02 states that the contract price to be paid to the contractor shall be adjusted based on the actual quantity executed under various items of work as per the schedule of items.

4. Article 5 of the agreement deals with the terms of payment. As per Clause 5.02, the assessee herein, as a contractor, would be given down payment of 10% of the contract price. Clause 5.03 states about the advance amount to be received by the contractor from the owner in respect of the materials to be used in the execution of the contract, namely, cement and steel. While the assessee herein would be entitled to receive 75% of the value of the cement, as far as steel brought to site for incorporation into the works was concerned, the assessee would be entitled to 100% payment. The clause further reads that the advance thus paid would be recovered from the monthly progress payments pro-rata according to the quantities of work billed for, to the extent of 75% of the cost of cement and 100% of the cost of steel. Clause 5.08 states that the progress payment made shall be regarded as payment by way of advance against final payment only and not as payment for the work completed till the date of progress payment. Clause 24.01 of the contract further provides that the contractor assessee herein had to arrange for all the materials required for the contract work, including steel and cement. Clause 24.02 states that on request from the contractor assessee, the owner might assist the contractor in procuring steel and cement and giving the contractor the necessary priority and essentiality certificates. Irrespective of the assistance of the owner, the contractor had the

responsibility to procure all materials, including steel and cement from whatever sources as might become necessary in advance to see that the execution of the work went on uninterrupted. Thus, procuring cement and steel and moving it to the site were the sole responsibilities of the assessee herein. On the basis of the said facts, the assessee claimed that the value of the closing stock, cement and steel could not be included as part of its income. The Assessing Authority, however, pointed out that the assessee had debited a sum of Rs.99,08,381/- towards the cost of steel, but it had credited to the earnings only a sum of Rs.43,35,400/-. The assessee had consumed Rs.47 lakhs worth of steel.

5. The Assessing Authority rejected the case of the assessee that the cost of cement supplied by NSTL would be shown as its income, only when it was adjusted against the R.A. bills submitted by the assessee and passed finally by the owner. Rejecting the said contention of the assessee, the Assessing Authority pointed out that since N.S.T.L. had already debited the assessee's account with the amount paid by them towards the cost of cement, the closing stock would be treated as the income of the assessee.

6. Aggrieved by this, the assessee went on appeal before the Commissioner of Income Tax (Appeals). Referring to Clause 5.03, the Commissioner of Income Tax (Appeals) held that the assessee had to pay for the cement and steel supplied by NSTL. In the circumstances, there could be no separate addition. Thus, the addition of a sum of Rs.55,72,981/- was cancelled.

7. The Revenue filed an appeal before the Tribunal as against this portion of the order, which, however, accepted the Revenue's contention and allowed the appeal. The Tribunal pointed out that when the assessee had undertaken only labour contract, the assessee should not have debited the cost of material to its account. Thus, without showing corresponding earnings, the cost of the material, per se, could not be claimed by the assessee in the accounts. In the circumstances, agreeing with the contention of the Revenue, the Tribunal allowed the Revenue's appeal, thereby restored the assessment. Aggrieved by this, the assessee is on appeal before this Court.

8. Heard learned counsel appearing for both sides and considered the material placed on record.

9. As rightly pointed out by the learned counsel appearing for the assessee, the entire contention of the Revenue rested on the wrong premise that the payment had been made by the owner - NSTL, a fact which is totally against the agreed terms of the contract between the assessee and NSTL. As already pointed out in the preceding paragraph, the contract contemplated supply of materials by the assessee for the execution of the contract. All that the agreement provided for under Article 5 was payment of advance money to the assessee by the owner for procuring the steel and cement, in which event, the assessee being the purchaser of the goods to be used in the execution of the contract, the advance money received by the assessee was adjustable in the final bill. As though this was supplied by NSTL during the year which had

not been accounted for, the Assessing Authority, however, misconstrued the said clause to hold that the difference between the consumption account debited and the earnings account credited should be assessed as earnings of the assessee of this year. As rightly pointed out by the Commissioner of Income Tax (Appeals), the clauses in the agreement clearly show that the assessee had to pay for the cement and steel used in the contract. The rest of the advance amount from NSTL cannot be, however, construed that NSTL paid for steel and cement. Going by the terms of the contract, particularly Clause 2.06 and Article 5, we have no hesitation in accepting the plea of the assessee that the Tribunal misconstrued the clauses in the agreement to hold that the value of the closing stock had to be treated as income of the assessee.

In the circumstances, we have no hesitation in setting aside the order of the Tribunal. Accordingly, the order of the Tribunal stands set aside and the Tax Case Appeal stands allowed. No costs.

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To

1. The Deputy Commissioner of Income Tax
Special Range IX
Chennai-600 034.
2. The Commissioner of Income Tax (Appeals)
Chennai.
3. The Income Tax Appellate Tribunal
Chennai B Bench