IN THE INCOME TAX APPELLATE TRIBUNAL
AHMEDABAD ñCòBENCH

Before: Shri Rajpal Yadav, Judicial Member
And Shri Amarjit Singh, Accountant Member

ITA Nos. 1902 & 2492/Ahd/2014
Assessment Year 2009-10 & 2011-12

The DCIT, Circle-4, Ahmedabad (Appellant)	Vs	Indo Colchem Ltd. Plot No 36/2, GIDC Estate, Phase-II, Vatva, Ahmedabad PAN: AAACI4393K (Respondent)

Revenue by: Shri Prasoon Kabra, Sr. D.R.
Assessee by: Shri Kishan M. Mehta, A.R.

Date of hearing : 17-01-2018
Date of pronouncement : 07-03-2018

आदेश/ORDER

PER : AMARJIT SINGH, ACCOUNTANT MEMBER:-

These two Revenueôs appeals for A.Y. 2009-10 & 2011-12, arise from order of the CIT(A)-VIII, Ahmedabad dated 10-03-2014, in proceedings under section 143(3) of the Income Tax Act, 1961; in short ñthe Actò.

2. The revenue has raised following grounds of appeal:-

ITA No. 1902/Ahd/2014

“1. The Ld.CIT(A) has erred in law and on facts in deleting the addition of Rs.2,24,64,664/- made on account of low net profit, without properly appreciating the facts of the case and the material brought on record.”

3. In this case, return of income declaring income of Rs. 1,14,00,998/- was filed on 30th September, 2009. Subsequently, the case was selected under scrutiny by issuing of notice u/s. 143(2) of the act on 28th September, 2010. The assessee company is engaged in the business of manufacturing of dies and dies intermediates and trading in chemicals. During the course of assessment proceedings, the assessing officer has noticed that assessee has shown gross profits of Rs 1,96,24,039/- @ 2.85% on sale of Rs. 68,92,45,395/-. In the immediate preceding year, the assessee had shown net profit of Rs. 2,45,92,180/- @ 4.03% on sale of Rs. 61,04,02,990/-. On scrutiny, the assessing officer has observed that assessee had included gain and loss from foreign exchange fluctuation in computing the profit of the business. However, he was of the opinion that gain and loss of foreign exchange was income from other sources, therefore, she has re-calculated the net profit for the year under consideration after excluding gain from foreign exchange fluctuation as the calculation made by the assessing officer is reproduced as under:-

> *"1. The Ld. CIT(A) has erred in law and on facts in deleting the addition of Rs.2,24,64,664/- made on account of low net profit, without properly appreciating the facts of the case and the material brought on record."*

	A.Y. 2009-10	*A.Y. 2008-09*
Sales	*Rs.68,92,45,395/-*	*Rs.61,04,02,990/-*
Net Profit	*Rs. 1,96,24,039/-*	*Rs. 2,45,92,180/-*
Less: Gain from Foreign Exchange Fluctuation	*Rs.61,39,020/-*	
Add: Loss from Foreign Exchange Fluctuation		*Rs.7,5 1,667/-*
Actual business Net profit	*Rs.61,39,020/- Rs.2,53,43,847/-*	

Net profit ratio	*0.89%*	*4.15%*

In view of the above, the assessing officer observed that the net profit of the assessee for the year under consideration was reduced by 3.26% on comparing to preceding assessment year 2008-09. Consequently, the assessing officer has taken the net profit for the year under consideration at 4.15% and made addition of Rs. 22464664/- to the total income of the assessee.

4. Aggrieved assessee filed appeal before the ld. CIT(A). The ld. CIT(A) has allowed the appeal of the assessee by observing as under:

"6.3 <u>Decision:</u>

I have carefully considered the facts of the case, the assessment order and the written submission of the appellant. The AO has estimated the net profit of the appellant company by adopting the percentage of net profits shown by the appellant in the preceding year after rejecting the books of accounts under section 145. it was observed by him that there was a discrepancy in respect of the accounts of two parties from which he made enquiries under section 133(6). He held that the appellant did not maintain its books of accounts properly and it was not showing true and fair income of the appellant company.

During the course of appellate proceedings the submissions given by the appellant were forwarded to the AO for his comment as there were certain new information in the explanations given by the appellant. The AO has commented that sufficient opportunity was given to the appellant during the course of assessment proceedings. The observations of the AO have been examined and it is noted that the objections raised by the AO are general in nature and no factual examination of the written submission has been made by the AO and he has not pointed out any errors in the explanation given by the appellant regarding this issue.

The appellant on the other hand, has submitted that the action of the AO in rejecting the books of accounts was not proper as the discrepancies were duly explained by it during the course of assessment proceedings and there was no further query from the AO. Further the computation of net profit rate by the AO was also erroneous.

The issue therefore, has two components, first; the rejection of books of accounts and the second; estimation of profit by comparing the net profit rate. It would be logical to examine the rejection of books of accounts first. The AO has rejected the books of account under section 145 as it was noted by him that the accounts of two parties obtained by him under section 133 (6) were not matching with the accounts maintained by the appellant in its books. However it is noted that the appellant has reasonably explained the difference, in one of the parties namely; Sheerfine Chem Pvt Ltd the difference of Rs. 8053 was on account of vatav kasar. The appellant has also furnished the copy of Ledger account and explain the difference. The information and explanation was given before the AO however it is noted from the assessment order that the AO has not given any finding in respect of this explanation by the appellant. Similarly the other party namely; Amardeep Dyes and Intermediates Ltd the difference had occurred as the appellant has booked the sales made to that party in the current financial year whereas *the other party has booked it in the year of receipt, that is, next year in the month of April when the goods were received. In my opinion the explanation given by the appellant regarding discrepancies in the books of accounts were acceptable. The nature of these defects are such that this cannot form the basis of rejection of books of accounts so as to conclude that the profits of the appellant company cannot be computed in a logical manner. The appellant company has duly explained the defects. Even otherwise had these defects been correct, the books of accounts could not have been rejected on this basis. It is also observed that the books are regularly audited and the audit report, does not contain any remark of the arbiter, auditor regarding any defect in the books of account. Therefore, the rejection of books of accounts by the AO under section 145 cannot be upheld. The action of the AO is accordingly set aside.*

Regarding the calculation of net profit calculations made by the AO it appears that the AO has made factual error in making the assessment. It would be useful to reproduce the calculations done by the AO for determining the net profit rate: -

	A.Y.2009-10	A.Y.2008-09
Sales	Rs.68,92,45,395/-	Rs.61, 04,02,990/-
Net profit	Rs. 1,96,24,039/-	Rs. 2,45,92,180/-
Less: Gain from Foreign Exchange fluctuation	Rs. 61,39,020/-	
Add: Loss from Foreign Exchange Fluctuation		Rs. 7,51,667/-
Actual business net profit	Rs.61 ,39,020/-	Rs.2,53,43,847/-
Net profit ratio	0.89%	4.15%

An examination of the above table will show that the AO has reduced the gain from foreign exchange fluctuation of Rs. 61,39,0207- from the net profits shown by the appellant during the year. A further examination of the profit and loss account submitted by the appellant shows that there was in fact a loss from foreign exchange fluctuation and same was claimed an expenditure by the appellant in the profit and loss account. The AO has therefore grossly erred in reducing the loss on account of foreign exchange fluctuation. It has resulted in double reduction of the net profit of the appellant. By correcting this error the net profit of the appellant company will increase by that amount. The table drawn by the AO can be redrawn as under: -

	A.Y.2009-10	A.Y.2008-09
Sales	Rs.68,92,45,395/-	Rs.6 1,04, 02,990/-
Net profit	Rs. 1,96,24,039/-	Rs. 2,45,92,180/-
Add: Gain from Foreign Exchange fluctuation	Rs. 61,39,020/-	
Add: Loss from Foreign Exchange Fluctuation		Rs. 7,51,667/-
Actual business net profit	Rs2,57,63,059/-	Rs.2,53,43,847/-

Net profit ratio	*3.73%*	*4.15%*

Therefore, it is clear from the above table that by correcting the error made by the AO the net profit ratio is almost comparable to the preceding year. The appellant has also explained that as compared to earlier year there were certain other expenses which the appellant had to additionally incur. It is explained that there was an increase in financial expenses of the company as the appellant had taken foreign exchange loan. There was an increase of Rs. 84.99 Lacs to 134.55 Lacs on interest expenses alone. Therefore considering these aspects the net profit shown by the appellant is comparable with the earlier years. Accordingly, the AO was hot justified in comparing the net profit in the manner that has been done in the assessment order. There are glaring factual errors in the order.

In view of the above facts and circumstances the addition made by estimating the net profit is directed to be deleted. The addition cannot be made as the rejection of books of accounts made by the AO was not proper and also there are glaring factual errors in the estimation of net profit.

The ground of appeal is accordingly allowed"

5. During the course of appellate proceedings before us, ld. departmental representative has supported the order of assessing officer. On the other hand, the ld. counsel has furnished paper book containing detailed submission made before ld. CIT(A), accounts of exchange rate fluctuation, month-wise rate of US doller, audited a/c etc. He had contended that reason for fall in the net profit of the assessee during the year under consideration was due to exchange rate variation as the US doller price in terms of rupees were not favourable.

6. We have heard both the sides and perused the material on record carefully. We observed that there is mistake in the calculation of the net profit by the assessing officer. The assessing officer has reduced the gain from foreign exchange fluctuation of Rs. 61,39,020/- from the net profit shown by the assessee during the year. In fact, there was loss from foreign exchange fluctuation and the same were claimed as expenditure by the assessee in the profit and loss accounts. The assessing officer has erred in reducing the loss on account of foreign exchange fluctuation. It is

clear from the findings of the ld. CIT(A) that after correcting the error made by the assessing officer, the net profit rate is almost comparable to the preceding year. In view of these facts, there is error in the estimation of net profit by the assessing officer. Therefore, we consider that ld. CIT(A) has correctly deleted the addition wrongly framed by the assessing officer as elaborated above. Accordingly, the appeal of the revenue is dismissed.

7. In the result, the appeal of the revenue is dismissed.

8. The revenue has raised following grounds of appeal:-

ITA No. 2492/Ahd/2014

"1. The Ld. CIT(A) has erred in law and on facts in deleting the addition of Rs. 36,73,466/- made on account of low net profit, without properly appreciating the facts of the case and the material brought on record."

9. In this case, return of income declaring income of Rs. 2,53,52,715/- was filed on 29th September, 2011. Subsequently, the case was selected under scrutiny by issuing of notice u/s. 143(2) of the act on 14th September, 2012. On scrutiny, the assessing officer has noticed that the gross profit of the assessee has increased from 12.49 to 12.67%. However, the net profit has fallen from 4.01% to 3.41%. The assessee has explained that the fall in net profit was because of increase in foreign cost by way of increase in exchange rate variation which resulted in fall in the net profit during the year under consideration. The assessing officer has not accepted the explanation of the assessee by stating that assessee has not explained the same with quantitative data, therefore, the assessing officer has assessed the net profit of the assessee at 4.01% as against 3.41% shown by the assessee and made addition to the amount Rs. 36,73,466/-.

10. Aggrieved assessee filed appeal before the ld. CIT(A). The ld. CIT(A) has allowed the appeal by observing as under:-

<u>"Decision:</u>
I have carefully considered the facts of the case, the assessment order and the written submission of the appellant. During the course of assessment proceedings it was noted by the A.O. that the GP shown by the appellant has increased marginally but there was a fall in net profit from 4.01% to 3.41% as compared to earlier years. The appellant explained that the fall in net profit rate was due to exchange rate variation. However, the AO did not accept the explanation given by the appellant and made an addition of Rs. 36,73,466/- for the difference on account of fall in net profit during the year.
It is also been observed by the AO that addition to total income was also made on similar grounds for A.Y. 2009-10.

The appellant on the other hand has explained that the net profit has fallen during the year as exchange rate variation for finance expenses of Rs.13.6 lakh was there during the year whereas earlier year there was an income of 50.89 Lacs. Since there was an income due to foreign exchange fluctuation in earlier year the net profit was higher in A.Y 2010 - 11 as compared to the present year. For A.Y 2009-10 there was a foreign exchange fluctuation expenditure and addition was made on that ground. The addition made in that year was deleted by first appellate authority. It has been submitted by the appellant that other expenses such as administrative and selling expenses were comparable to earlier years. The appellant has also pointed out that no defect or discrepancies have been found in the books of accounts on verification by the AO and there was no material or reason to hold that the accounts of the appellant were not correct and complete. It has therefore, been requested by the appellant that the addition made should be deleted.

On careful consideration of the entire facts of the case, it Is noted that the addition on account of fall in net profit rate was also made in the case of the appellant in A. Y.2009 - 10. While deciding the appeal for that year I have held that no addition on account of comparison of net profit can be done as the appellant had clearly explained that the fall in net profit was due to variation of foreign exchange rates. In that year the addition was made by comparing the net profit with A Y 2008 - 09. It was explained by the appellant that in A. Y 2008 - 09 there was a gain due to foreign exchange fluctuation whereas in A.Y 2009 -10 there was a loss on account of foreign exchange fluctuation. This has happened as the appellant had taken foreign exchange loan. The facts of the case at hand are similar to that year. In the present year also the appellant has incurred a loss of Rs. 13.6 Lacs as against the income of 52.77 Lacs immediately preceding year. If the variation due to foreign exchange fluctuation is removed the net profit becomes comparable. It has been rightly pointed out by the appellant that the rate of foreign exchange mainly US dollar varied from Rs. 50.22 to Rs. 45.14 during FY 2009 -10 which resulted in income due to fluctuation. The appellant has also given comparison of expenses of various years which show that the expenses are more or less in similar proportion as compared to other years. It is also noted that no material defect in the books of accounts have been found out by the AO before rejecting the book results. The AO has held that the appellant did not supply the quantitative data of foreign exchange rate variation. It has

> *been held by him that unless quantitative data were verified the contention of the appellant regarding fall in net profit rate cannot be accepted and accordingly the books of accounts were rejected. The findings given by the AO are not justified. Books of accounts cannot be rejected mainly in absence of one information. It is noted that the books of accounts are duly audited and the auditors have not recorded any specific defect which was noted by them during the course of audit of the books of accounts of the appellant.*
>
> *In view of the above discussion it is held that no addition on account of fall in net profit rate can be made to the income of the appellant. The addition made by the A.O. is, therefore, directed to be deleted.*
>
> *The ground of appeal is accordingly,* ***allowed."***

11. We have heard rival contentions and perused the material on record carefully. It is undisputed fact that during the year under consideration there was loss of Rs.13.60 lacs due to foreign exchange rate variation whereas in the earlier year there was an income of Rs. 50.89 lacs because of foreign exchange fluctuation. The above facts demonstrate that the reason for fall in the net profit during the year was on account of incurring foreign exchange loss during the year compared to tremendous profit earned in the earlier year on account of foreign exchange fluctuations. Therefore we are inclined with the findings of the ld. CIT(A).Accordingly the appeal of the revenue is dismissed.

12. In the result, the appeal of the revenue is dismissed.

13. In the combined result, both the appeals of the revenue are dismissed.

Order pronounced in the open court on 07-03-2018

Sd/-	**Sd/-**
(RAJPAL YADAV)	**(AMARJIT SINGH)**
JUDICIAL MEMBER	**ACCOUNTANT MEMBER**

Ahmedabad : Dated 07/03/2018

<u>आदेश की प्रतिलिपि अग्रेषित</u> <u>/ Copy of Order Forwarded to:-</u>

1. Assessee
2. Revenue
3. Concerned CIT
4. CIT (A)
5. DR, ITAT, Ahmedabad
6. Guard file.

By order/आदेश से,

उप/सहायक पंजीकार

आयकर अपीलीय अधिकरण,

अहमदाबाद