IN THE INCOME TAX APPELLATE TRIBUNAL "A" BENCH : CHENNAI

[Before Hon'ble Shri NRS Ganesan, JM & Hon'ble Shri M.Balaganesh, AM]

I.T.A Nos. 2027 & 2028/CHNY/2017

Assessment Year : 2005-06 & 2006-07

Citadel Fine Pharmaceuticals(P) Ltd. [PAN: AAACC1356 N]	-vs-	ACIT, Circle-I(3), Chennai
(Appellant)		(Respondent)

For the Appellant : Shri S. Sundararaman, CA

For the Revenue : Shri ARV Sreenivasan, JCIT

Date of Hearing : 17.01.2018

Date of Pronouncement : 08.02.2018

ORDER

Per M.Balaganesh, AM

1. These appeals by the Assessee arise out of the common orders of the Learned Commissioner of Income Tax(Appeals)-5, Chennai [in short the ld CIT(A)] in Appeal Nos.72 & 73/CIT(A)-5/13-14 dated 20.06.2017 against the orders passed by the ACIT, Circle-I(3), Chennai[in short the ld AO] under section 143(3) of the Income Tax Act, 1961 (in short "the Act") dated 11.12.2007 and 15.12.2011 respectively for the Assessment Years 2005-06 and 2006-07 respectively. Both the appeals are taken up together and disposed off by this common order for the sake of convenience.

ITA No. 2027/CHNY/2017 – Asst Year 2005-06 – Assessee Appeal

2. The first issue to be decided in this appeal is as to whether the ld CITA was justified in upholding the disallowance of Rs 1,18,23,353/- towards sales promotion expenses in the facts and circumstances of the case.

2.1. The brief facts of this issue is that the assessee company is a manufacturer of pharmaceutical goods. It incurred a sum of Rs 1,18,23,353/- as Sales Promotion expenses in respect of its products. The assessee entered into a Joint Venture Agreement dated 27.3.2002 with another company by name Citadel Aurobindo Biotech Limited (CABL in short) as a result of which it had sold its brands to the said company. It was agreed between the assessee and CABL, that they would reimburse the assessee certain sales promotion expenses incurred in respect of its branded products and therefore, the assessee had not debited the related sales promotion expenses to the profit and loss account in the year of its incurrence. The fact that these expenses were genuinely incurred and that it was recoverable from CABL was not in dispute at all. The asseseee was having various correspondences with CABL for over three years. Ultimately, CABL refused to reimburse the said sum of Rs 1,18,23,353/- during the Asst Year 2005-06. In other words, the refusal was made by CABL in Asst Year 2005-06 and accordingly the assessee decided to write off the said claim in its books of accounts and accordingly wrote off the same in Asst Year 2005-06 and claimed the same as a deduction. The ld AO observed that the assessee had furnished the entire list of expenses made on account of sales promotion expenses. The assessee submitted that these were expenses incurred by it in Asst Year 2002-03 immediately before the assessee's brands were sold to its Joint Venture Company CABL. The assessee actually incurred the expenditure towards promotion of its brands for various products and since the said brands were sold by the assessee to CABL, it was decided by the assessee to treat the same as recoverable from CABL and accordingly reflected in the same under the head 'Current Assets' in the

Balance Sheet of Brand division. These current assets were also subject to be taken over by CABL on actual historical cost. The assessee pleaded that since CABL refused the claim of assessee to take over the sales promotion expenses of Rs 1,18,23,353/- incurred towards Brand division , and that this refusal came to light only in the Asst Year 2005-06 , the assessee had no other option but to write off the same in the books of accounts and claim as deduction. The assessee also pleaded that no deduction was claimed by the assessee with regard to these sales promotion expenses in the year of actual incurrence. It was only due to take over of Brand division and repeated correspondences that were exchanged to resolve the dispute with regard to take over of this claim of sales promotion expenses, no deduction was claimed in the earlier years. Since the dispute could not be resolved for over three years and that the same got resolved only in Asst Year 2005-06 by clearly knowing from CABL that they are not willing to absorb this expenditure, it was decided to write off in the books of assessee as irrecoverable loss incidental to business in Asst Year 2005-06 and deduction was claimed accordingly in the return.

2.2. The ld AO went through the entire correspondences between the assessee and CABL that were placed on record before him. He came to a conclusion that the reply of the assessee cannot be accepted for the reasons that as per the letter issued by CABL on 31.1.2005, it is observed that CABL has rejected the payment of the above claim of the assessee for the following reasons:-

> *"a) The expenses for the cited amount was never mentioned in the Agreement for purchase a Brands and taken over of Current Assets, dated 27.03.2002.*
>
> *b) The argument that Compliments of Gift articles constitute a part of the Current Assets taken over cannot be applied to your claim for the simple reason that there was no proper accounting available for the same and all have been reported to have been distributed well before the formation of the JV Company.*
>
> *c) Also, we feel that since promotion of products constitute a daily routine there is nothing extra-ordinary in giving compliments/gifts to doctors. As far as we can foresee, this is akin to paying the salary to your staff.*

d) More importantly, the talk of forming a JV was initiated only sometime in November-December, 2001 and when the items were ordered there was no linking that a JV company was in the anvil.

e) Your claim looks like an additional levy on us for the purchase of your brands and we are unable to appreciate the points referred to in your letter dated 03.02.2003.

f) Books like Ha Ha Therapy' though authored by a renowned doctor is more a book on 'humour during medicine practice' rather that giving any insight into technicalities. However, since, you had your own strategies we do not want to comment further on this.

g) Again, Diary for 2002 definitely is not for any product promotion and can be only for the sake of corporate image.

h) Samples and compliment being treated in the same plane for the sake of the agreement cited above is rather amusing. First of all, we cannot treat them alike for the simple reason that the compliments/gifts have been distributed, already.

i) We have considered samples that were available as current assets. You should understand that we have not considered samples given away prior to the formation of the JV as current assets nor even what is available with the Field Staff during the chage-over".

Based on the aforesaid reasons, the ld AO held that the expenses were not related to CABL as claimed by the assessee. The ld AO further held that the sales promotion expenses were incurred during the Asst Year 2002-03 and hence were not related to earning of income for the Asst Year 2005-06. The ld AO held that claim of the assessee is wrongly placed and cannot be accepted as expenditure of the current year and disallowed sales promotion expenses of Rs 1,18,23,353/- in the assessment.

2.3. Before the ld CITA, the assessee narrated the facts of the case together with the various correspondences that were submitted before the ld AO and submitted that the loss got crystallized only during the Asst Year 2005-06 and it is akin to loss incidental to the business and should be allowed as deduction u/s 28 of the Act. The ld CITA placed reliance on the CBDT Circular No. 5/2012 dated 1.8.2012 wherein it was held that business expenditure incurred in providing freebies to medical practitioner by pharmaceutical and allied health sector industry is not an allowable deduction u/s 37(1)

of the Act. He stated that as per Medical Council of India (MCI) regulations dated 10.12.2009 imposes a prohibition on the medical practitioner and their professional associations from taking any gift, travel facility, hospitality, cash or monetary grant from the pharmaceutical and allied health sector industries. The ld CITA based on this circular concluded that the subject mentioned sales promotion expenses incurred by the assessee would be hit by prohibition imposed by Medical Council of India and hence the explanation to section 37(1) of the Act would come into play. The ld CITA held that the expenditure incurred by the assessee in Asst Year 2002-03 would be in the nature of freebies, gifts etc given to doctors which is prohibited as per statute (i.e MCI regulations). Accordingly, he held that the disallowance had been rightly made by the ld AO.

2.4. Aggrieved, the assessee is in appeal before us on the following grounds :-

2. The Commissioner of Income Tax (Appeals) erred in treating a disputed claim written-off by the Appellant amounting to Rs. 1,18,23,353/- on the ground that: a) the expenditure not incurred wholly and exclusively for the purpose of the business; and b) the expenditure is even otherwise disallowable in terms of the CBDT Circular 5/2012 in F. No. 225/142/2012-ITAT.II dated 1st August, 2012.

3. The Commissioner of Income Tax (Appeals) erred in disregarding to the basic fact that the appellant had made a legitimate claim in pursuance of an Agreement with an company (Citadel Aurobindo Biotech Limited) to which it had sold its brands and that both the amount incurred and the claim made were never in dispute.

4. The Commissioner of Income Tax (Appeals) erred in not taking into consideration that the amount written off is a disputed claim between two parties and the decision to write off was justifiably taken during the year of account and hence, the amount written off should be allowed as a loss incidental to the business.

5. The Commissioner of Income Tax (Appeals) erred in disregarding the fact that even-though Citadel Aurobindo Biotech Limited had initially (as per the terms of the agreement) agreed that they would reimburse the Appellant certain sales promotion expenditures incurred by it (during the year of sale of the brands i.e.

assessment year 2002-03) they subsequently did not reimburse the expenditure incurred and hence the amount written off partook the nature of a claim and not of a sales promotion expenditure as concluded by the Commissioner of Income Tax (Appeals).

6. The Commissioner of Income Tax (Appeals) erred in considering the fact that the aforesaid claim is not an expenditure of the Appellant, and, hence, the CBDT Circular has no application.

7. Even assuming the loss claimed by the Appellant were to be treated as an expenditure incurred of the appellant, the Commissioner of Income Tax (Appeals) erred in not considering the fact that the aforesaid CBDT Circular (relied by him) was issued only on 1st August, 2012 consequent to the amendments made (on 10th December, 2009) in the provisions of Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulations, 2002 (the "Regulation") and since the expenditure incurred by the Appellant was much prior to the date of the Circular of the CBDT/amendment in the Regulations, Circular of the CBDT has no application.

2.5. We have heard the rival submissions and perused the materials available on record. We find that the assessee had entered into a joint venture agreement dated 27.3.2002 with another company by name CABL as a result of which, it had sold its brands to the said company for a total sum of Rs 19 crores. As per para 5 of the said agreement for purchase of brands and take over of current assets, it was agreed that CABL would reimburse the assessee certain sales promotion expenses incurred in respect of branded products and , therefore, the assessee had not debited the related sales promotion expenses incurred by it during the Asst Year 2002-03 to its profit and loss account. We find that the fact of incurrence of these expenses for the purpose of business and its genuinity thereon were not disputed by the revenue. The assessee was trying to resolve the dispute with regard to absorption of these expenditure in the books of CABL and various correspondences in this regard were entered into over a period of three years which are part of the records. We find that CABL however refused to pay the amount claimed by the assessee and the decision with regard to non-payment was communicated to the assessee only during the Asst Year 2005-06 and hence the assessee had no other

option but to write off the same as irrecoverable loss in its books of accounts and claim deduction for the same. Even though the ld AO accepted the facts relating to the claim made by the assessee and that it was genuine business expenditure, he disallowed merely on the ground that the same were incurred in the earlier previous year relating to Asst Year 2002-03 and cannot be allowed in Asst Year 2005-06. In other words, the disallowance was made by the ld AO by treating the said expenditure as prior period expenses. But we find that the necessity to absorb the said expenditure in Asst Year 2005-06 (i.e the year under appeal) got crystallized only pursuant to the letter rejecting the claim dated 31.1.2005 by CABL, which falls in Asst Year 2005-06. As long as the necessity of the business expenditure and genuinity thereon had not been disputed by the revenue and more so in view of the fact that no deduction towards the same were claimed by the assessee in the year of its incurrence, we have no hesitation to hold that the said expenditure would be allowable as a deduction pursuant to rejection by CABL vide letter dated 31.1.2005 and by appreciating the fact that the irrecoverability of the expenditure leading to loss got crystallized only in Asst Year 2005-06 in the hands of the assessee herein. Moreover, the ld AO had given a categorical finding that the subject mentioned disputed expenditure does not pertain to CABL. It is not the case of the revenue that the said sales promotion expenses were incurred for non-business purposes of the assessee. The only reason for disallowance by the ld AO was that it pertains to prior period , which aspect has already been addressed by us hereinabove. We would like to place reliance on the allowability of prior period expenses as deduction on the following decisions :-

a) Hon'ble Delhi High Court in the case of CIT vs Jagatjit Industries Ltd reported in (2011) 339 ITR 382 (Del)

b) Delhi Tribunal in the case of Sony India (P) Ltd vs DCIT reported in (2008) 118 TTJ 865 (Del Trib)

2.5.1. Coming to the alternative argument taken by the ld CITA in his order that expenses incurred by the assessee would be hit by the CBDT Circular No . 5/2012 , we hold that

the aforesaid CBDT Circular 5/2012 in F.No. 225/142/2012-ITA.II was issued on 1.8.2012 pursuant to MCI regulations dated 10.12.2009, whereas the expenditures were incurred in the instant case were incurred much prior to it. We find that the decision relied upon by the ld DR in the case of *Confederation of Indian Pharmaceutical Industry vs CBDT rendered by Hon'ble Himachal Pradesh High Court reported in (2014) 44 taxmann.com 365 (HP) dated 26.12.2012* actually advances the case of the assessee. The only ground raised before the court was that Circular No. 5/2012 dated 1.8.2012 issued by CBDT is to be quashed as it goes beyond the section itself. The Hon'ble Court in its decision was not required to decide on the nature of expenditures which all are in violation of the regulations framed by the MCI. Infact, the Hon'ble Court has held that –

> *" The regulation of the medical council prohibiting medical practitioners from availing of freebies is a very salutary regulation which is in the interest of patients and the public. This court is not oblivious to the increasing complaints that the medical practitioners do not prescribe generic medicines and prescribe branded medicines only in lieu of the gifts and other freebies granted to them by some particular pharmaceutical industries. Once this has been prohibited by the Medical Council under the powers vested in it, section 37(1) comes into play. The Petitioner's contention that the circular goes beyond the section is not acceptable. In case the assessing authorities are not properly understanding the circular then the remedy lies for each individual assessee to file an appeal but the circular which is totally in line with section 37(1) cannot be said to be illegal. If the assessee satisfies the assessing authority that the expenditure is not in violation of the regulations framed by the medical council then it may legitimately claim a deduction, but it is for the assessee to satisfy the AO that the expense is not in violation of the Medical Council Regulations."*

In the instant case, it is not the case of the ld AO that the expenditures incurred in the form of giving diaries, medical planners, medical representative bags etc were in the nature of expenditure prohibited by MCI regulations. In any event, these expenditures were incurred much prior to the introduction of the CBDT Circular and MCI regulations itself. We have already held that the genuinity of the expenditure and business purposes thereon were not doubted by the revenue herein. Hence we hold that the decision relied

upon by the revenue supra actually supports the case of the assessee. We further hold that the applicability of the Circular 5/2012 could only be prospective in nature and cannot be made applicable for the Asst Year under dispute before us. Reliance in this regard has been rightly placed by the ld AR on the co-ordinate bench decision of *Ahmedabad Tribunal in the case of ITO vs Sunflower Pharmacy reported in (2017) 88 taxmann.com 326 dated 22.12.2017 for Asst Year 2011-12*, wherein it was held that the Circular No. 5/2012 is applicable only from Asst Year 2013-14 only. We also find that the co-ordinate bench of this tribunal in the case of M/s Vasantha Subramanian Hospitals P Ltd vs DCIT in ITA No. 2345/Mds/2015 for Asst Year 2012-13 dated 22.4.2016 had held as under:-

> *"16. After hearing both sides, we find merit in the contention of the learned Authorized Representative. There is no prohibition in the Act to make payments to Doctors for the services rendered by them. In the case of the assessee, gifts were given to Doctors by way of gold coins in appreciation to their services. It can be construed as the fees paid in kind for the services rendered by the Doctors in the hospital. The presumption of the learned Assessing Officer that these payments are made to Doctors for canvassing patients cannot be accepted without any cogent evidence. Further the Revenue has not quantified the amount for which invoices, bills are not available for the expenditure incurred and the nature of unexplained expenses. Hence, it appears to be a passing remark. Therefore, in the interest of justice, we hereby direct the learned Assessing Officer to delete the addition made on account of disallowance of Rs. 71,62,741/-."*

The aforesaid decision also supports the facts of the instant case.

2.5.2. In view of our aforesaid facts and findings and respectfully following the judicial precedents relied upon hereinabove, we allow the claim of write off of the assessee in the sum of Rs 1,18,23,353/- as deduction in Asst Year 2005-06. Accordingly, the Grounds 2 to 7 raised by the assessee for Asst Year 2005-06 are allowed.

3. The next issue to be decided in this appeal is as to whether the ld CITA was justified in confirming the addition made u/s 41(1) of the Act in the sum of Rs 39,90,797/- in the facts and circumstances of the case.

3.1. The brief facts of this issue is that the assessee showed amounts payable to M/s Citadel Aurobindo Biotech Ltd (CABL in short) in its balance sheet as on 31.3.2005. The ld AO observed that CABL is a group concern of the assessee. The ld AO observed that since CABL had ceased its business operations, he came to a conclusion that the assessee would not pay the dues to CABL and accordingly invoked the provisions of section 41(1) of the Act by stating that the said liability ceased to exist. The assessee pleaded that CABL is also assessed by the very same assessing officer assessing the assessee herein. The assessee pleaded that CABL had reflected the very same balance as has been reflected by the assessee and there is no dispute regarding the same. The assessee stated the amount of Rs 39,90,797/- is the net amount due to CABL which is also reflected as receivable in the books of CABL. The confirmation to this effect from CABL was also filed before the ld AO. Hence it was pleaded that there is no intention to terminate the liability and that the said liability had not ceased to exist so as to invoke the provisions of section 41(1) of the Act. The ld AO however proceeded to invoke section 41(1) of the Act by ignoring the submissions of the assessee and made an addition to the tune of Rs 39,90,797/-in the assessment.

3.2. The ld CITA placed reliance on the decision of the Hon'ble Punjab & Haryana High Court in the case of Mrs Adarsh Sood vs CIT reported in (2014) 47 taxmann.com 268 (P&H) and confirmed the addition on the ground that the assessee did not disagree or disprove the fact brought on record by the ld AO that CABL ceased to exist.

3.3. Aggrieved, the assessee is in appeal before us on the following ground:-

> *8. The Commissioner of Income Tax (Appeals) erred in sustaining an addition u/s 41(1) of the Act amounting to Rs. 39,90,797/- due by the Appellant to Citadel Aurobindo Biotech Limited on the ground that the liability ceased to exist even though the Appellant proved to the Commissioner of Income Tax (Appeals) Citadel Aurobindo Biotech Limited continues to exist even till date and that there*

is nothing on record to show that Citadel Aurobindo Biotech Limited had waived its claim.

3.4. We have heard the rival submissions. The ld AR argued that the ld AO had only brought on record the fact that operations of CABL had been ceased and not that CABL itself ceased to exist. We find lot of force in this factual submission made by the ld AO as is evident from the wordings used by the ld AO in his order. Accordingly, we hold that the decision relied upon by the ld CITA is squarely distinguishable on facts . When the entire balance outstanding in the sum of Rs 39,90,797/- is reflected as receivable in the books of CABL, which is also assessed by the very same AO, there cannot be any cessation of liability on the part of the assessee. We find that the ld AO had only forced the assessee to cease the liability payable to CABL. Had the ld AO verified the records of CABL which is also assessed in his office / circle only, he could have understood the truth. Without doing the same, the action of the ld AO by making an addition u/s 41(1) of the Act is not warranted and accordingly deserves to be deleted. Accordingly, the Ground No. 8 raised by the assessee is allowed.

4. The last issue to be decided in this appeal is as to whether the ld CITA was justified in upholding the disallowance made u/s 40(a)(ia) of the Act towards audit fees in the facts and circumstances of the case.

4.1. The brief facts of this issue is that the assessee made provision for audit fees of Rs 2,52,909/- and claimed the same as deduction. But this expenditure was not subjected to deduction of tax at source. Accordingly, the ld AO sought to disallow the same u/s 40(a)(ia) of the Act for violation of provisions of section 194J of the Act. The assessee replied that the audit fees, though expenses, of the year of account, the amount is payable only after the signing of the report by the auditor, and therefore, till it is signed, it will not be known as to whom the amount has to be paid. It was submitted that the provisions of section 194J of the Act would not apply to audit fees, as the question of payment to the

auditor would arise only after the signing of the accounts which takes place after the year end. The ld AO however proceeded to disallow the same u/s 40(a)(ia) of the Act which was upheld by the ld CITA. Aggrieved, the assessee is in appeal before us on the following ground:-

> *9. The commissioner of Income Tax (Appeals) erred in sustaining an addition on account of provision of audit fees without considering the fact that audit fees, though an expense, of the year of account, the amount is payable only after the signing of the audit report by the auditors and, therefore, till it is signed, the amount provided in only a provision and not a liability and therefore the provisions of sec. 40(a)(ia) of the Act would not apply in such a case.*

4.2. We have heard the rival submissions. On perusal of section 194J of the Act, we find that tax is deductible at source either at the time of credit of expenditure to the account of the payee or at the time of payment whichever is earlier. In the instant case, the assessee had made provision for audit fees to the account of the payee which fact has been mentioned by the ld CITA. Hence the provisions of section 194J of the Act are clearly attracted and non-deduction of tax at source would automatically invite disallowance u/s 40(a)(ia) of the Act. The statutory auditor is appointed in the annual general meeting of the company by the shareholders and would hold office till the conclusion of the next annual general meeting. Hence the name of the payee (i.e the auditor) is very well known to the assessee in order to make provision for audit fees by crediting to the said auditor's account. Admittedly the audit fees is an item of expenditure claimed by the assessee as an expenditure incurred on accrual basis during the year under appeal and this is made only based on the auditor's appointment made in the annual general meeting or in any other extraordinary general meeting , as the case may be. Hence we are not inclined to accept the arguments of the ld AR that the audit report is signed after the end of the year. Accordingly, the Ground No. 9 raised by the assessee is dismissed.

ITA No. 2028/Mds/2017 – Asst Year 2006-07

5. The assessee has challenged the validity of reopening of assessment made by the ld AO in this appeal apart from challenging the addition made thereon on merits. Before we go into the merits, we deem it fit to addresss this preliminary issue of validity of reopening the assessment. The assessee has raised the following ground in this regard:-

> *6. The Appellant submits that the reopening of the assessment made by the Assessing Officer is not correct for there was no fresh material available with the Assessing Officer to reopen the assessment – for the reopening has been made based on the documents filed with the return of income.*

6. The brief facts of this issue is that the assessee company filed its return of income for the Asst Year 2006-07 electronically on 16.8.2007 admitting loss of Rs 73,832/-. No assessment was framed on the said return u/s 143(3) of the Act. This assessment was later sought to be reopened by issuance of notice u/s 148 of the Act on 24.2.2011 on the following reasons :-

> *During the year, the assessee has offered Long Term Capital Gains of Rs 1,77,106/- . The same is set off against business losses of Rs 2,50,938/-. The assessee company had shut down its business and the return of income electronically filed exhibits lack of business activity and hence, the expenditure akin to business cannot be allowed and the entire capital gains of Rs 1,77,106/- needs to be taxed.*

The reassessment was framed u/s 143(3) r.w.s. 147 of the Act on 15.12.2011 by making an addition of Rs 11,09,690/- to the closing stock of raw materials and taxable income of Rs 10,35,860/- determined as under:-

Business loss	- (-) Rs	2,50,938/-
Capital Gains	- Rs	1,77,106/-
Loss Returned by the assessee	(-) Rs	73,832/-
Add: Addition made in reassessment	- Rs	11,09,690/-
Income Assessed in Reassessment	Rs	10,35,858/-
Rounded off to	Rs	10,35,860/-

6.1. During the re-assessment proceedings, the ld AO took the value of closing scrap for the current Asst Year on the basis of scrap sales made in the Asst Years 2008-09 and 2009-10 of raw materials and packing materials at Rs 11,09,690/- and added the above sum to the taxable income of Asst Year 2006-07. The assessee submitted that during the Asst Year 2006-07, the stock values of its raw materials and packing materials have been valued at Rs Nil applying the principle of cost or net realizable value whichever is lower as enumerated in Accounting Standard (AS) 2 issued by The Institute of Chartered Accountants of India (ICAI). It was pleaded that in pharmaceutical industry, every product has a pre-determined expiry date and since the products were expiered, the net realizable value of such stocks has been considered at Rs Nil. As regards packing materials, since there is no sale of finished goods, the packing materials consisting of cardboard boxes, aluminium foil wrappers, blister packing sheets etc can be only sold as scrap. The assessee submitted that it is an admitted fact that the sale value of Rs 11,09,690/- appearing in Asst Years 2008-09 and 2009-10 is scrap sales realized and not on sale of finished goods. The scrap value of any stock cannot be ascertained on an earlier date and can be only known upon actual realization of scrap sales since they don't have any pre-set market readily available for sale. It is also an admitted fact that the assessee was able to sell the scrap only after 3 years. According the assessee objected to the adoption of value of closing stock based on information which is actually available in Asst Years 2008-09 and 2009-10 and not relevant for Asst Year 2006-07 (i.e the year under appeal). The ld AO however, did not heed to these contentions of the assessee on merits and made an addition of Rs 11,09,690/- in the re-assessment, which was also confirmed by the ld CITA. Aggrieved, the assessee is in appeal before us .

6.2. The ld AR argued that the dispute in this appeal is in respect of the following:- (i) reopening of assessment u/s 147 of the Act ; (ii) bringing to tax a new source of income without even discussing in his order the issue for which the assessment has been reopened and (iii) valuing closing stock (classified as scrap) based on scrap sales made in

Asst Years 2008-09 and 2009-10. The ld AR further argued that there was no fresh material for reopening and the ld AO had initiated proceedings u/s 147 of the Act merely on change of opinion on matters already considered which is not valid in law as held by the Hon'ble Supreme Court in the case of Kelvinator of India Ltd reported in 320 ITR 561 (SC). He pleaded that no disallowance / addition was made in the reassessment in respect of reasons recorded (i.e disallowance of business loss) by the ld AO. Hence he argued that the entire re assessment deserves to be quashed. In response to this, the ld DR vehemently relied on the orders of the lower authorities.

6.3. We have heard the rival submissions. At the outset, we find that the reopening was made for the Asst Year 2006-07 for disallowance of business loss of Rs 2,50,938/- as in the opinion of the ld AO, the assessee did not carry on any business activity and hence the business expenditure incurred thereon leading to arising of business loss is to be disallowed and once the same is done, the Long Term Capital Gain of Rs 1,77,106/- returned by the assessee would get taxed separately. But we find from the re-assessment order, the ld AO had accepted the claim of business loss of Rs 2,50,938/- accepting the fact that the assessee had carried on business activity and no disallowance was made to that effect. We find that the provisions of Explanation 3 to section 147 of the Act empowers the ld AO to reopen the assessment, if , he has reason to believe, that any income chargeable to tax has escaped assessment for the relevant year, 'and also bring to tax' , any other income, which may attract assessment, though, it is brought to his notice, subsequently, albeit, in the course of reassessment proceedings. We would like to lay emphasis on the expression 'and also bring to tax' appearing in the main part of section 147 of the Act in relation to the right of the ld AO to assess taxable income discovered during reassessment proceedings. Thus in the reassessment proceedings, it is not permissible for the ld AO to tax any other source of income unless the ld AO assesses to tax that income with reference to which the ld AO had formed reason to believe that it had escaped assessment. In the instant case, the purported income ie valuing the closing

stock of scrap which was discovered subsequently during the course of reassessment proceedings , can be brought to tax, only if the escaped income i.e business loss claimed by the assessee, which triggered, in the first instance, the issuance of notice u/s 148 of the Act, is assessed to tax. As stated above, during the reassessment proceedings, the ld AO agreed with the contentions of the assessee that it had indeed done business activity and hence the business loss was allowed to be set off with other income. In this scenario, the ld AO would be precluded from making any other addition towards the new source of income as prima facie his reason to believe that income had originally escaped assessment had failed. We draw support from the following decisions of various High Courts in this regard :-

a) Hon'ble Bombay High Court in the case of CIT vs Jet Airways Ltd reported in 331 ITR 236 (Bom) .

b) Hon'ble Delhi High Court in the case of Ranbaxy Laboratories Ltd vs CIT reported in 336 ITR 136 (Del) .

c) Hon'ble Calcutta High Court in the case of CIT VS Infinity Infotech Parks Ltd in ITAT No. 60 of 2014 G.A.No. 1736 of 2014 dated 10.9.2014.

d) Hon'ble Jurisdictional High Court in the case of Martech Peripherals P Ltd vs DCIT and Another reported in (2017) 394 ITR 733 (Mad) dated 4.4.2017

6.4. Even on merits, from the facts narrated and explanations given hereinabove , we find that the ld AO is not justified in valuing the closing stock of packing materials representing scrap based on the scrap sales made in subsequent years ignoring the principles of valuation of stock as enumerated in AS 2 issued by ICAI which is also mandated to be followed u/s 145A of the Act. Hence no addition towards valuation of closing stock could be validly made in the reassessment even on merits in the instant case.

6.5. In view of our aforesaid findings in the facts and circumstances of the case and respectfully following the various judicial precedents relied upon hereinabove, we hold

that the re-assessment proceedings framed for the Asst Year 2006-07 deserves to be quashed. Accordingly, the grounds raised by the assessee for the Asst Year 2006-07 are allowed.

7. In the result, the appeal of the assessee in ITA No. 2027/Mds/2017 for Asst Year 2005-06 is partly allowed and appeal of the assessee in ITA No. 2028/Mds/2017 for Asst Year 2006-07 is allowed.

Order pronounced in the Court on 08.02.2018

Sd/-	Sd/-
[NRS Ganesan]	[M.Balaganesh]
Judicial Member	Accountant Member

Dated : 08.02.2018
SB, Sr. PS

Copy of the order forwarded to:
1. Citadel Fine Pharmaceuticals (P) ltd., 43, Main Road, Velachery, Chennai-42
2. ACIT, Circle-I(3), Chennai-34.
3..C.I.T.(A), Chennai4. C.I.T.- Chennai.
5. CIT(DR), Chennai Benches, Chennai.

True copy

By Order

Senior Private Secretary
Head of Office/D.D.O., ITAT, Chennai Benches