No addition under sec. 145 if AO failed to find defects either in books or in accounting method

Summary – The Jodhpur ITAT in a recent case of Drillcon (Raj) (P.) Ltd., (the Assessee) held that where Assessing Officer did not point out any specific defect in books of account or method of accounting consistently followed by assessee and no inflated purchases or suppressed sales or expenses not incurred for business purposes were found, provisions of section 145(3) were not applicable.

Facts

- The Assessing Officer having found that the assessee had not proportionally disallowed expenses relating to insurance on goods in transit, freight and handing entry-tax (purchase, and channel finance bank interest, rejected books of account maintained by the assessee and made upwards adjustment in closing stock.
- The Commissioner (Appeals) confirmed addition made by the Assessing Officer and also upheld the rejection of books of account under section 145(3).
- On second appeal :

Held

Valuation of closing stock

- It is noticed that the Assessing Officer made the impugned addition by invoking the provisions of section 145(*3*) however; no specific defects have been pointed out in the books of account maintained by the assessee in regular course of its business. The Assessing Officer did not point out any inflated purchase or suppressed sales. The claim of the assessee was that the expenses considered by the Assessing Officer for increasing the value of the closing stock had already been debited in the books of account and those expenses were directly related with the purchases because insurance on goods in the transits was incurred to cover the transit risk and the expenses were already debited as part of the purchase, therefore, not to be added while valuing the closing stock.
- All the expenses which were added by the Assessing Officer on proportionate basis for the valuation of closing stock were already included in the purchase and the method of valuation of the assessee was cost or market price whichever was less. This fact is also clear from col. 12(*a*) in form 3 CD which is part of tax audit report under section 44AB. In the said column the auditor mentioned that the valuation by the assessee is "at cost including direct expenses or market value whichever is less". It is also mentioned in Col. 12(*b*) that there was no deviation in the above method. It is also an admitted fact that the department has accepted the tax audit report and pointed out no discrepancy in the said report. Therefore, the Assessing Officer was not justified in making the addition in the

valuation of the closing stock particularly when the same valuation of the stock had also been accepted by VAT authorities and Commercial Tax Officer in their respective assessment orders.

- In the present case, it is also noticed that for assessment year 2004-05 the assessment was framed under section 143(*3*) after making proper scrutiny and valuation of the closing stock was accepted, during the year under consideration, there is no deviation in valuing the closing stock from the method of valuation accepted by the Department in assessment year 2004-05, so there was no occasion to make addition in the year under consideration as expenses pointed out by the Assessing Officer were already included by the assessee in the cost of purchase and the stock available with the assessee was out of purchase. Therefore, the proportionate amount of the expenses which was already recorded in the books of account as those were directly linked to the purchase, added by the Assessing Officer in the valuation of closing stock, was not correct.

Rejection of books of account

- In the present case, the Assessing Officer while rejecting the books of account of the assessee by invoking the provisions of section 145(*3*) had not given any other reason except the observation that the proportionate expenses incurred by the assessee on account of insurance on goods in transit, freight and handling, entry tax (purchase) and channel finance interest, were to be added. The Assessing Officer did not point out any specific defect in the books of account or the method of accounting consistently followed by the assessee. It is also not the case of the Assessing Officer that there was a deviation in valuing the closing stock in comparison to the earlier year, no inflated purchases or suppressed sales or expenses not incurred for the business purposes was found. Even the gross profit declared by the assessee on turnover which was higher in comparison to earlier year, has not been doubted by the Assessing Officer. Therefore, the provisions of section 145(*3*) were not applicable to the facts of this case and Commissioner (Appeals) was not justified in confirming the impugned addition made by the Assessing Officer.