IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCHES : D : NEW DELHI

BEFORE SHRI R.S. SYAL, VICE PRESIDENT
AND
MS SUCHITRA KAMBLE, JUDICIAL MEMBER

ITA No.2552/Del/2011
Assessment Year : 2005-06

DCIT, Circle-18(1), Room No.211A, CR Building, New Delhi.	Vs.	UOP India (P) Ltd., Unitech Trade Centre, 1st Floor, Sector-43, Block C, Sushant Lok, Phase-I, Gurgaon. PAN: AAACU2687E

Assessee By	:	Shri S.K. Agarwal, CA
Deptt. By	:	Shri Umesh Chand Dubey, Sr. DR

Date of Hearing	:	27.04.2017
Date of Pronouncement	:	28.04.2017

ORDER

PER R.S. SYAL, VP:

This is an appeal filed by the Revenue against the order passed by the CIT(A) on 28.02.2011 in relation to the assessment year 2005-06.

2. The only ground raised in this appeal is against the deletion of addition of Rs.3,76,16,855/- made by the Assessing Officer by applying net profit rate of 8.68% as against 2.5% shown by the assessee.

3. Briefly stated, the facts of the case are that the assessee is engaged in providing technical and engineering services and also execution and supply of equipments for large projects in the field of refinery for domestic and overseas projects. Return declaring income of Rs.1.04 crore was filed. The Assessing Officer observed that the net profit rate shown by the assessee at 2.51% for the instant year was much lower than 11.03% and 12.50% of the immediately two preceding years. On being called upon to explain the reasons for decline in the net profit, the assessee submitted that there was increase in cost of sales on certain products which was negotiated some time back, but, were executed during the current year and also there was increase in depreciation due to capitalization of

leasehold improvements and purchase of new assets during the year. The Assessing Officer did not accept the assessee's justification for decline in the net profit rate by finding that no stock register was maintained by it; no details of gross profit rate for the last two years and current year were provided; the reply furnished by the assessee towards increase in cost of sales and increase in depreciation was vague. He, therefore, invoked the provisions of section 145. Net profit rate shown by the assessee in two earlier years was averaged at 8.68%. Such net profit rate was applied on the turnover of the assessee to the tune of Rs.60.97 crore for making an addition of Rs.3,76,16,855/-. The assessee filed certain additional evidence before the ld. CIT(A) justifying the reasons for decline in the net profit rate. Such additional evidence was sent to the Assessing Officer for remand report. After considering the remand report and also the assessee's reply to the remand report along with other relevant material, the ld. CIT(A) deleted the addition by observing that the books of account were not rightly rejected by the Assessing Officer and, hence, the addition was not sustainable. The Revenue is aggrieved against the deletion of addition.

4. We have heard the rival submissions and perused the relevant material on record. Before taking up the issue on merits, it is relevant to mention that the ld. DR strongly objected to the admission of additional evidence in contravention of rule 46A. He relied on certain decisions in support of his point. We are not inclined to accept this objection, firstly because there is no such ground taken in the memorandum of appeal, and secondly, the additional evidence accepted by the ld. CIT(A) was duly confronted to the AO, whose remand report was also obtained. As such, we cannot accept the objection of the ld. DR.

5. On merits, the assessee has a combined stream of revenue from projects as well as from services. There is no demarcation in the accounts indicating the incurring of

expenses for a particular source of revenue. The Assessing Officer rejected the accounts and made the addition mainly because of decline in the net profit rate for the instant year as against the preceding years and then because the assessee did not maintain any stock register.

6. From the perusal of accounts, we find that the assessee is not carrying any inventory. Neither, there is any opening stock nor a closing stock. The assessee is booking purchase of material and spares directly to the projects upon incurring itself. As the assessee is not having any stock, there can be no question of maintaining any stock register.

7. The nature of business carried on by the assessee is such that there cannot be any consistency in the rate of profit over the years. The Assessing Officer objected to 'Unbilled revenue of uncompleted contracts' reflected by the assessee in its balance sheet at Rs.1,47,85,384/-. Such objection was taken during the course of remand proceedings. The Assessing

Officer opined that this much amount should have been brought to tax. Here, it is relevant to mention that the assessee is following percentage completion method. Revenue is booked in the accounts corresponding with the percentage of completion of project. If, for example, the assessee has incurred a cost of Rs.100/- on one particular project, the assessee also recognizes revenue in respect of such cost of Rs.100/- irrespective of the fact whether such revenue has been billed or not. This amount of Rs.1.47 crore as shown in the balance sheet is unbilled revenue on uncompleted contracts which was included by the assessee in its overall figure of revenue taken to the Profit & Loss Account. In the subsequent year when the assessee will issue invoice for the amount, the corresponding amount appearing in the balance sheet for the instant year will get reversed. It, therefore, transpires that the unbilled revenue, adversely considered by the Assessing Officer is, in fact, an item of income duly offered by the assessee for taxation.

8. The Assessing Officer has, then, objected to a debit of Rs.70,39,513/- in the assessee's Profit & Loss Account with the narration 'Estimated loss on incomplete contract.' The assessee is regularly following this pattern of estimating loss on incomplete contracts and booking such loss in its Profit & Loss Account. If a contract was entered into an earlier year whose execution started a little later, there is bound to be increase in the cost without there being any corresponding increase in the revenue. The assessee recognizes such estimated loss on incomplete contracts in consonance with the Accounting Standards by giving the corresponding credit in that balance sheet under the head 'Provision for estimated loss on incomplete contracts.' In a subsequent year, when the contract is completed, such provision is reversed and the actual profit or loss is deduced. This method of recognizing loss of incomplete contracts has been consistently followed by the assessee, which has never been objected in the past. In this view of the matter, there cannot be any objection to such

debit in the Profit & Loss Account. Quantum of such loss has not been disputed by the AO.

9. It is further relevant to note that the assessee vehemently argued before the authorities below that some of the contracts which were entered into in earlier years got concluded in the instant year and the revenues fell much short of costs. This was shown by way of a table which has been reproduced on page 7 of the impugned order as below:-

Project Name	Project Revenue	Project Cost	Profitability	%
IOCL Aromatics (agreement executed on July 12, 2002)	214	232.6	(18.6)	(9.00)
BPCL Merox (agreement executed on March 23, 2004)	70	75	(5)	(7.00)

10. It can be seen from the above project-wise table covering nearly 75% of the total revenue of the assessee for the instant year that the project costs far exceeded the project revenues and the assessee incurred loss of Rs.23.6 million from these two projects. This loss has impacted the ultimate profit of the

assessee. This position has not been controverted by the Assessing Officer even in the remand proceedings.

11. Apart from that, the assessee explained before the Assessing Officer that there was increase in the assets which resulted in higher depreciation and, ultimately, low net profit. This objection was also not taken into consideration whose effect is that there is an additional debit of Rs.1.06 crore on this account.

12. If the effect of the above extraordinary items is taken away, the net profit rate of the assessee turns out to be 18.39%, as against 2.51% as under:

Particulars	Amount [as per audited financial statements]	Amount [excluding the impact of items mentioned below]
Total Turnover	609,710,648	609,710,648
Less: Project Revenue (IOCL &BPCL)	-	(280,000,000)
Turnover (excluding IOCL and BPCL revenue [A]	-	329,710,648
Total cost	594,404,618	594,404,618
Less: Project Cost (IOCL	-	(307,671,880)

&BPCL)		
Less: Estimated loss on incomplete contracts as per AS-7	-	(7,039,513)
Less : Depreciation on assets added during the year	-	(10,609,582)
Cost (excluding items mentioned above) [B]	-	269,083,643
Net Profit [C=A-B]	15,306,030	60,627,005
Net Profit as a % of Turnover [C/A*100]	2.51	18.39

13. It is apparent that the extraordinary items have reduced the net profit of the assessee to 2.51%. It goes without saying that when there is a genuine decline in the net profit rate for the reasons which are as obvious as are prevalent in the prevalent case, there can be no rejection of books of account. We, therefore, hold that the AO was not justified in rejecting the books of account.

14. It is pertinent to note the assessee's net profit rate for nine years which have been tabulated on page 6 of the impugned order as under:-

A.Y.	Turnover	Net Profit in Rs.	Net Profit Rate (as a % of turnover) C=(B/A)*100
2008-09	760,614,230	22,408,295	2.95
2007-08	539,863,913	38,850,923	7.20
2006-07	516,727,612	37,610,084	7.28
2005-06	609,710,648	15,306,029	2.51
2004-05	466,410,865	51,428,933	11.03
2003-04	462,907,308	57,879,953	12.50
2002-03	193,478,333	2,863,156	1.48
2001-02	301,335,322	24,684,053	8.19
2000-01	80,680,170	4,883,528	6.05

15. It can be seen from the net profit rates that there is a wide fluctuation from as low as 1.48% to as high as 12.50%. There is no consistency in the profit rates. The assessee declared NP rate of 2.95% for the A.Y. 2008-09 which has been accepted by the Assessing Officer in assessment made u/s 143(3) of the Act. A copy of such order has been placed on record.

16. In view of the foregoing discussion, we are of the considered opinion that the ld. CIT(A) was fully justified in deleting the addition.

17. In the result, the appeal is dismissed.

Order Pronounced in the open Court on 28.04.2017.

Sd/-	Sd/-
[SUCHITRA KAMBLE] JUDICIAL MEMBER	[R.S. SYAL] VICE PRESIDENT

Dated, 28th April, 2017.

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Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT (A)
5. DR, ITAT

AR/NEW DELHI.