

(2005) 08 CAL CK 0084
In the Calcutta High Court
Case No : IT Appeal No. 67 of 2001

Ashoke Refractories (P) Ltd.

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

Date of Decision : 08-08-2005

Acts Referred:

Income Tax Act, 1922 — Section 13
Income Tax Act, 1961 — Section 145

Citation : (2005) 199 CTR 115 : (2005) 279 ITR 457 : (2005) 148 TAXMAN 635

Hon'ble Judges : Maharaj Sinha, J;D.K. Seth, J

Bench : Division Bench

Advocate : J.P. Khaitan, Sanjay Bhowmick and C.S. Das, for the Appellant;M.P. Agarwal and S.N. Dutta, for the Respondent

Final Decision : Allowed

Judgement

D.K. Seth, J.—The question :

In this appeal the question to be answered is as follows :

"Whether the Tribunal was justified in law in holding that the GP of the appellant for the asst. yrs. 1990-91 and 1991-92 should be calculated at the GP of the asst. yr. 1989-90 at 18.71 per cent and whether the purported findings of the Tribunal in this behalf are based on any material and/or have been arrived at by ignoring the relevant materials and/or by taking into consideration irrelevant and/or extraneous materials and/or are otherwise arbitrary, unreasonable and perverse ?"

The facts :

2. In this case the assessment years involved are 1990-91 and 1991-92. The AO had found so far as the year 1990-91 is concerned that no stock register or production register was maintained by the assessee. Item-wise quantity of goods produced, the opening stock, the closing stock, the purchases and the sales were not verifiable. The stocks are sold at different rates revealing that the same stock

was sold at a lower rate and also at a higher rate and that the assessee was unable to explain the item-wise production of different kinds of bricks and failed to explain the fall in average sale figure compared to the last year and the revised Tax Audit Report was also silent about the yield of finished products by commenting "not ascertained" and the AO ultimately came to the conclusion that it was clear that the assessee had failed to establish the correctness of the income deduced on the basis of the accounts maintained by the assessee.

2.1 The CIT(A) reversed the order. The learned Tribunal affirmed the order. It is against this order the present appeal has been filed. Similar is the case in respect of the asst. yr. 1991-92, though, however, the facts are little different with which we will deal at appropriate stage.

The submission : The appellant/assessee :

3. Mr. J.P. Khaitan, senior counsel, assisted by Mr. Sanjay Bhowmick appearing on behalf of the appellant, submits that the rejection of the books of account was not justified having regard to the proviso to Section 145 as it stood prior to its amendment applicable to the relevant assessment year. The absence of stock register itself would not justify the rejection of the books of account unless coupled with certain other factors. According to him, there were materials from which even without the stock register the accounts could be verified. He also points out that there was no finding to the extent that the accounts were not correct and complete or that the AO was of the opinion that the income could not be deduced from the accounts maintained by the assessee. In the absence of such conclusion, the books of account could not be rejected. To support his contention, he relied on *Pandit Bros. Vs. Commr. of Income Tax*, , *S. Veeraiah Reddiar Vs. Commissioner of Income Tax, Travancore-Cochin, Bangalore*, , *P. Venkanna Vs. Commissioner of Income Tax, Mysore*, , *R.V.S. and Sons Dairy Farm Vs. Commissioner of Income Tax*, and *Omar Salay Mohamed Sait Vs. Commissioner of Income Tax, Madras*, . He also relied on *S.N. Namasivayam Chettiar Vs. The Commissioner of Income Tax, Madras*, cited by Mr. Agarwal to support his contention.

3.1 The next contention that was raised alternatively by Mr. Khaitan was, that assuming but not admitting that the books of account were rightly rejected, in that event, in order to arrive at the income, the Tribunal could not have proceeded simply on the basis of the figures of earlier sales related to earlier years ignoring the other materials placed before it on the basis of which the income could not be presumed to be shown less, particularly when the learned Tribunal had accepted that the price had gone down and the price of raw materials had gone upward. On this ground, he prays that the order of the learned Tribunal be set aside.

3.2 He also points out that so far as the asst. yr. 1991-92 is concerned, there was stock register. But on the ground that it has not been maintained item-wise, therefore, the accounts were rejected. However, even in the assessment order or

the order of the learned Tribunal, there was no opinion expressed that the method applied was such that from the accounts maintained the income could not be deduced though the accounts were not found to be incorrect or incomplete. Therefore, according to him, the books of account could not at all be rejected.

The submission : The respondent/Department:

4. Mr. Agarwal, learned Counsel for the Department, on the other hand, contended that the materials clearly show that there were discrepancies in the stock register and the vouchers and there were materials before the AO and the learned Tribunal to lead a reasonable person to take one or the other view and in such a case it cannot be said that the finding arrived at by the learned Tribunal was perverse. The finding of facts arrived at by the learned Tribunal being concluded finding of facts cannot be disturbed by the High Court dealing with substantial questions of law. He also points out that though not in clear terms but from the materials placed before the Court it can very well be said that the AO and the learned Tribunal had expressed a view that the income could not be deduced from the accounts maintained. He also pointed out that the assessee had shown income disproportionate to the sale figures without any justification as to why the income should fall down in comparison with the earlier years. He points out that though the AO had taken the average of the earlier years but the learned Tribunal had taken the lowest of the earlier three years. Therefore, there is no perversity. He relied on the decision in *S.N. Namasivayam Chettiar v. CIT* (supra), *Commissioner of Income Tax Vs. Surjit Singh Mahesh Kumar*, , *Awadhesh Pratap Singh Abdul Rehman and Brothers Vs. Commissioner of Income Tax*, , *Dhondiram Dalichand Vs. Commissioner of Income Tax, Poona*, and *Amiya Kumar Roy and Bros. Vs. Commissioner of Income Tax*, to support his contention.

The scope:

5. We have heard the learned Counsel for the respective parties. The question to be determined on the basis of the facts disclosed before us is as to whether the AO and the learned Tribunal was justified in rejecting the books of account or that in the facts and circumstances of the case the books of account could be rejected. In case we find that the books of account could not be rejected, then we need not go into the other questions raised in this case.

5.1 In the circumstances, we propose to deal with the first point as to whether the rejection of the books of account were justified or not or could be so done having regard to the facts and circumstances of this case.

Section 145 : Scope : The present case : Whether the accounts could be rejected : 6. Section 145 of the IT Act, 1961, as it stood prior to its amendment, applicable to the relevant assessment years provided that where the accounts are correct and complete to the satisfaction of the AO but the method employed is such that in the opinion of the AO the income cannot properly be deduced therefrom, then the computation can be made upon such basis and in such a

manner as the AO may determine.

6.1 In this case, it was not held by the AO nor the learned Tribunal that the accounts maintained were not correct and complete. On the other hand, it had proceeded to reject the accounts on the ground that the assessee had failed to establish the correctness of the income deduced on the basis of the accounts maintained by the assessee, so far as the asst. yr. 1990-91 is concerned. The law is well settled. In order to reject the books of account, the AO has to come to an opinion that the method applied is such that the income cannot properly be deduced from the accounts so maintained. It is not a question of establishment by the assessee. It is the opinion of the AO, which is material. In order to arrive at such a conclusion, it must be shown that the AO has taken into consideration the various factors and has not omitted to consider the materials before him and has come to a conclusion that the method applied is such that from the accounts the income could not be deduced.

6.2 In the present case, as pointed out by Mr. Khaitan, it is not in dispute that these goods were excisable goods and that regular monthly returns used to be submitted before the excise authority. Mr. Khaitan drew our attention to pp. 110-116 and 118-124 of the paper book. From the said materials, which were produced before the learned Tribunal, it appears that these were returns submitted to the excise authority giving full description of the goods and these were maintained on the basis of the books of account and were verified. There is no allegation that excise duty was avoided. Therefore, from these materials the accounts could be deduced having regard to the accounts reflected in the books of account. He has also drawn our attention to various other materials, which are part of the paper book. Therefrom, it appears that the regular accounts were being maintained. He has also referred to a conciliation of the accounts at pp. 63-64 (paper book), which were also before the IT authority. Our attention was also drawn to various notes of accounts, which were available on records and the audit report at pp. 65-70 (paper book) before the learned Tribunal. After having gone through these materials, we are of the view that only on the ground of absence of the stock register, so far as the asst. yr. 1990-91 is concerned, it cannot be held that in accounts maintained are such that the income could not be deduced, and therefore, the books of account could not be rejected.

6.3 At the same time, so far as the asst. yr. 1991-92 is concerned, it appears from the assessment order itself that the books of account, stock book of raw materials and finished goods were produced on 8th Feb., 1994, and were scrutinized (p. 128 paper book). It was found there by the learned Tribunal that from the stock book, it appears that there were three stages, (i) preparation of mixture of fire clay, (ii) mixed raw materials, and (iii) semi-finished product. It was also found that a month-wise chart was also given. But the AO observed that for certain months, viz., May, June, July and September, the weight of the semi-finished product was higher than the weight of the raw materials consumed. According to him, this was impractical. But a calculation, if made, shows that the

raw materials for April and May added together weighed 1,545 whereas the semi-finished product added to weigh 1,357 for these two months and similarly, till the months of June, July, August, calculated from April, shows to be 2,220 as weight of raw material and 2,123 as weight of semi-finished product for June; similarly, 2,821 and 2,754, respectively, for July and 3,702 and 3,575, respectively, for August. Therefore, it cannot be said that the semifinished product weighed more than the raw materials available with the assessee.

6.4 In any event, ultimately, there is no finding that in the opinion of the AO, the methods applied were such that the income could not be deduced from the books of account maintained by the assessee or that the accounts were not correct or complete. The learned Tribunal, on the other hand, had based its order on the ground that the reasons given in the order of the GIT(A) for the asst. yr. 1991-92, for deleting the addition made by the AO were not matching with those of the AO given in the assessment order. The difference of reason cannot be a factor for disagreeing with the decision by the CIT(A). The question is dependent on the principle of law. The question is to be determined on the basis of the fact applying the principle of law in the context in which the learned Tribunal is supposed to answer the question.

6.5 In the present case, the question is as to whether the books of account could be rejected only in the absence of stock register so far as the asst. yr. 1990-91 is concerned and on the grounds that the item-wise stocks were not maintained in the stock register could be a ground sufficient to reject the books of account for the asst. yr. 1991-92 without any finding that the accounts were incomplete or were incorrect or that though the accounts were complete and correct, but the methods applied were such that the income could not be deduced. Without a finding or forming an opinion to the extent indicated in expressed terms in the section itself, the books of account cannot be rejected merely in the absence of stock register or failure to maintain item-wise stock in the stock register when there were other materials available from which income could be deduced. In a case where books of account are so rejected without, the ingredients of Section 145 being fulfilled, such rejection is perverse and void.

6.6 Having regard to the facts and circumstances of the case as discussed above, in our view, the books of account for the asst. yrs. 1990-91 and 1991-92 could not be rejected and as such the order of the learned Tribunal in both the cases is liable to be set aside.

6.7 We may draw support for our views from the decisions relied upon by Mr. Khaitan. In *Pandit Bros. v. CIT* (supra), the Punjab High Court in a Division Bench held that in order to reject the accounts, the ITO must either hold that there was no method of accounting or that the method employed was such that it did not disclose the true profit and loss of the firm. In that case, the accounts maintained were accepted as correct, but only in the absence of stock register, the accounts were rejected. The learned Court held that the absence of stock register was not such a serious defect in the method of accounting employed by

the assessee that the ITO could not determine the correct statement of profits and losses. This decision was dealing with Section 13 of the IT Act, 1922, which is *pari materia* the same as Section 145 stood at the relevant point of time viz., before the amendment. In the said decision, it was further held that there must be material before the ITO to lead him to the conclusion that the method employed was defective or that the income could not be deduced. In the said decision, it was further held that the profits were low was merely a warning to the ITO to look into the accounts more carefully and to show whether there was material to conclude that there was something false in the account books. The mere fact that the profits were low was not material upon which a finding u/s 13 can be based, because the assessee may be incompetent or his method of business may be uneconomic. The mere fact that there was no stock register would not lead to hold that the account books were false. The books of account having been accepted as correct and disclosing a true state of affairs, the absence of one register cannot amount to be material and there must be a clear finding before the ITO could apply provisions of the proviso to Section 13. The Court cannot "leap in the dark" as was held by the Privy Council in *CIT v. Maharajadhiraja Kameshwar Singh of Darbhanga* (1933) 1 ITR 94.

6.8 In *Omar Salay Mohamed Sait v. CIT* (supra), it was held that if the Tribunal arrives at its own conclusion of facts after due consideration of the evidence before it in respect of a finding of fact, the Court is not supposed to interfere. However, that every fact for or against the assessee must be considered with due care and the Tribunal must give its finding clearly indicating the questions that arose for determination and the evidence pro and contra and thereafter reach the findings. The conclusions reached by the Tribunal should not be coloured by any irrelevant considerations or matters of prejudice. The Tribunal cannot base its findings on suspicions, conjectures or surmises, nor it can act on improper rejection of materials partly on evidence and partly suspicions, conjectures or surmises and if it so does, the finding is required to be set aside.

6.9 In *S. Veeriah Reddiar v. CIT* (supra), the Kerala High Court had held that low profits and absence of variety-wise or regular stock register were not sufficient reason or material on the strength of which the accounts of the assessee could be rejected under the proviso to Section 13 of the 1922 Act. Unless there is a finding against the assessee as to whether he had been regularly employing a method of accounting or where his income, profits and gains could not properly be deduced from his method of accounting, if he has been regularly employing a method of accounting, the accounting cannot be rejected. In *P. Venkanna v. CIT* (supra), dealing with the question of low profit had held that would not itself be a reason for disbelieving accounts.

6.10 In *R.V.S. & Sons Dairy Farm v. CIT* (supra) (the Court was) dealing with the question as to whether the average income was the right method where there were no books of account. However, we need not deal with this decision. On the other hand, Mr. Khaitan placed reliance on *S.N. Namasivayam Chettiar v. CIT*

(supra) cited by Mr. Agarwal to contend that non-production of stock register and manufacturing accounts when the assessee maintained regular accounts would not form the basis for rejecting the accounts, particularly, when there were other materials from which the income could be deduced. It is only if after taking into account all the materials including the one of stock register, it was found that (from) the method of accounting the correct profits of the business were not deducible, the operation of the proviso to Section 13 of the 1922 Act would be attracted. If after taking into account, in any case the absence of stock register coupled with other materials, the ITO was of the opinion that the correct profits and gains cannot be deduced, then there would be justification to attract Section 13 of the 1922 Act.

6.11 On the other hand, Mr. Agarwal wanted to rely upon S.N. Namasivayam Chettiar (supra) to contend that the absence of stock register was justifiable for rejecting the books of account in the facts and circumstances of the case. We, however, do not think that Mr. Agarwal was correct in his submission having regard to the facts and circumstances of this case and the ratio decided in S.N. Namasivayam Chettiar (supra). The reliance on Dhondiram Dalichand v. CIT (supra) also does not help Mr. Agarwal having regard to the facts and circumstances of the case, wherein it was held that in order to reject the accounts, the AO has to consider the facts and circumstances of the case and come to the conclusion that the method of accounting employed was such that the income could not properly be deduced therefrom. Similarly, the reliance on Amiya Kumar Roy & Bros. v. CIT (supra) does not seem to be apt in the facts and circumstances of the present case. There it was held that the failure to maintain stock accounts was a substantial defect in the accounts and that such finding is a finding of fact, which cannot be interfered with, having regard to the question referred to the Court. The facts being distinguishable from the present one, we do not think that the said decision can help Mr. Agarwal.

6.12 The ratio decided in CIT v. Surjit Singh Mahesh Kumar (supra) also does not help us in the present context, in view of the distinguishing feature and the question answered in the said case. Similarly, the decision in Awadesh Pratap Singh Abdul Rehman & Bros. v. CIT (supra) also does not apply in the present case in view of the fact that there it was held that the account books were rejected that there was no stock register and the sales were found unverifiable in the absence of the cash memos. The vouchers of expenses were also not forthcoming. The income returned was ridiculously low as compared to the exorbitant turnover and the extent of the business carried on by the assessee. Taking all these aspects and the materials into consideration, the Tribunal had found in the said case on fact that the claim of the assessee for acceptance of the account books was not sustainable and that such finding was a finding of fact and no question of law arose therefrom. But, in this case the facts were distinguishable viz., that the Tribunal had come to a finding after considering all other materials available, it was not possible to deduce the income in view or on account of the method of accounting employed by the assessee. Therefore, this

decision has not laid down any ratio that the absence of stock book would itself be sufficient to reject books of account.

Conclusion :

7. For all these reasons, the rejection of the books of account only in the absence of stock register for the year 1990-91 as discussed above having regard to the availability of other materials from which the income could be deduced, the rejection of the books of account by the learned Tribunal was contrary to the proviso to Section 145 unless there is a finding or opinion either that the records were incorrect and incomplete or that the method applied was such that the income could not be deduced from the accounts maintained by the assessee.

7.1 In respect of the asst. yr. 1991-92, the stock register was there, but only on the ground that the item-wise stock register was not maintained, the accounts were sought to be rejected, which is absolutely perverse and cannot be sustained in the absence of any opinion expressed or any finding arrived at that the accounts maintained were incorrect or incomplete or that the method of accounting applied was such that the income could not be deduced. In the absence of any such finding, the account books could not be rejected merely on the ground that item-wise stock was not maintained in the stock register.

Order:

8. In the result, the appeal, therefore, succeeds and is allowed. The order of the learned Tribunal is hereby set aside. The order of the CIT(A) is upheld and affirmed. The question involved in this appeal is answered in the negative for the first part and for the second part in the affirmative.

8.1 There will, however, be no order as to costs.

Maharaj Sinha, J.

9. I agree.