
(2005) 03 MP CK 0079
In the Madhya Pradesh High Court
Case No : MA (IT) No. 20 of 2001

Commissioner of Income Tax

APPELLANT

Vs

C.L. Khatri

RESPONDENT

Date of Decision : 29-03-2005

Acts Referred:

Finance Act, 2002 — Section 158BB

Income Tax Act, 1961 — Section 113, 132, 132A, 143, 143(3)

Citation : (2005) 197 CTR 44 : (2006) 282 ITR 97 : (2005) 147 TAXMAN 652

Hon'ble Judges : R.V. Raveendran, C.J.;Shantanu Kemkar, J

Bench : Division Bench

Advocate : Rohit Arya and Sanjeev Tuli, for the Appellant; A.P. Shrivastava, for the Respondent

Final Decision : Dismissed

Judgement

R.V. Raveendran, C.J.—This appeal by the Revenue u/s 260A of the IT Act, 1961 ("Act" for short), is against the order dt. 21st May, 2001 of the Tribunal, Indore Bench, in ITA No. (SS) 63/Ind/1997 for the block asst. yrs. 1987-88 to 1997-1998 (that is for the period 1st April, 1986 to 18th Oct., 1996).

2. In the appeal memo, the Revenue has raised as many as seven substantial questions of law for consideration. However, having regard to the fact that in regard to matters covered by questions (iii) and (vii), the Tribunal had set aside the issue and sent it back to the AO and the AO by order dt. 28th March, 2002, has already decided afresh questions (iii) and (vii), it was submitted that only question Nos. (i), (ii), (iv), (v) and (vi) which are extracted below, remain for consideration :

"(i) Whether, on the facts and circumstances of the case, the learned Tribunal was justified in law in holding that the matters disclosed in the returns filed for the relevant assessment years falling in the block period could not be investigated in the block assessment u/s 158BC ?

(ii) Whether, on the facts and circumstances of the case, the learned Tribunal was justified in law in deleting the additions made for undisclosed household expenditure for the asst. yrs. 1988-89 to 1996-97 and in directing the AO to re-examine the issue of undisclosed household expenses for the asst. yr. 1997-98 afresh ?

(iii) xxxxx

(iv) Whether, on the facts and circumstances of the case, the learned Tribunal was justified in law in deleting the addition of Rs. 14,673 made on account of suppression of net profit for the asst. yr. 1992-93 ?

(v) Whether, on the facts and circumstances of the case, the learned Tribunal was justified in law in deleting the addition of Rs. 20,000 made on account of unexplained investment in fixed deposits in the name of Master Rahul Khatri, Ku. Kanchan Khatri and Smt. Sonia Manwani ?

(vi) Whether, on the facts and circumstances of the case, the learned Tribunal was justified in law in deleting the addition of Rs. 19,180 made on account of unexplained cash found in the course of search ?

(vii) xxxxx"

3. The appeal had been admitted on 12th April, 2002 on the ground that the following substantial question of law arises for consideration (apart from the substantial questions of law framed in ITA Nos. 5, 7, 8 and 114 of 2001) :

"Whether, in the facts and circumstances of the case, the Tribunal was justified in setting aside the block assessment in respect of the assessee ?"

When the matter was taken up for hearing, both counsel submitted that the above question may not be appropriate as the block assessment was not set aside by the Tribunal in toto. They submitted that questions (i) and (ii) as suggested by the appellant (Revenue) may be considered instead of general question mentioned in the order dt. 12th April, 2002. It was also fairly conceded that questions (iv), (v) and (vi) are pure questions of fact and do not involve any question of law, as is evident from the questions themselves. Therefore, arguments were addressed and the appeal is disposed of only with reference to questions (i) and (ii).

4. There was a search and seizure operation in the case of the assessee who was the proprietor of "Kanchan Engineering" (and two others--Asandas and Purshottam Khatri) which commenced on 18th Oct., 1996 and completed on 30th Oct., 1996. The AO passed an assessment order dt. 29th Oct., 1997 in respect of the block period 1st April, 1986 to 18th Oct., 1996 under Chapter XIV-B.

5. One of the loose slips found at the time of such search related to "Kanchan Engineering". It showed the calculation of household expenditure as Rs. 14,000 in addition to Rs. 24,000 as the cost of ticket to Dubai. The assessee, when asked to explain, stated that the expenditure was per year and not for a month.

He also stated that his wife and mother had also drawn amounts for household expenses and there was no suppression of expenses or income. In regard to ticket to Dubai, the explanation was that it was borne by his brother. The AO found that the assessee had visited Dubai almost twice in a year and even the expenditure between Bhopal-Bombay and back and miscellaneous expenses may be around Rs. 10,000 per trip, or Rs. 20,000 per year. Relying on the said slip, the AO concluded that the household expenses of Rs. 14,000 was per month and not per year. As the said slip did not bear any date, he treated the slip as relating to the year in which it was found, that is accounting year 1996-97. Therefore, for the asst. yr. 1997-98, he calculated the household expenditure as 1,68,000. In regard to the previous years, he calculated the household expenses by deducting 10 per cent per year from the expenditure determined for 1997-98 considering the inflation rate as 10 per cent. He also added expenditure of Rs. 20,000 for Dubai visit for each year and arrived at the household expenditure plus Dubai expenditure as follows :

Srl.	Assessment	Total household	Withdrawals	Difference	No. year	expenditure
		shown by assesses	(determined as determined by AO for household undisclosed as per loose slip expenditure while expenditure) (Rs.)	filing return (Rs.)	(Rs.)	
1.	1987-88	78,320	11,680	66,640	2.	1988-89 84,920 11,200 73,720
3.	1989-90	92,150	19,000	73,150	4.	1990-91 1,00,160 13,600 86,560
5.	1991-92	1,09,040	14,100	1,03,930	6.	1992-93 1,18,880 14,950 1,03,930
7.	1993-94	1,29,920	15,750	1,14,170	8.	1994-95 1,42,160 35,900 1,06,260
9.	1995-96	1,56,080	22,100	1,33,980	10.	1996-97 1,71,200 29,000 1,42,200
11.	1997-98	1,18,000	15,000	1,03,000		

(Note : For the asst. yr. 1997-98 the expenditure was reckoned till October, 1996 that is Rs. 14,000 x 7 =98,000 + 20,000=1,18,000 less Rs. 15,000)

6. The assessee being aggrieved by the addition of the said amounts (and certain other additions) to the total income, filed an appeal before the Tribunal, Indore Bench. The assessee contended that the undisclosed income that could be assessed under Chapter XIV-B was "any money, bullion, jewellery or other valuable article or thing or any income based on any entry in the books of account or other, documents or transactions" (where such money, bullion, jewellery, valuable article, thing, entry in the books of account or other document or transaction represent wholly or partly income or property which has not been or would not have been disclosed for the purpose of the Act) having regard to the definition of "undisclosed income" in Section 158B(b) of the Act. The assessee further contended that in the returns with computation of income filed by him every year, he had shown the withdrawals towards household expenses and the same had been accepted by the AO; and that once a particular issue had been examined by the AO, it cannot be reopened by the AO while framing the block assessment unless there is some incriminating evidence with regard to the income or claim of the assessee in a particular assessment year. It was contended that whatever document was seized in the course of search proceedings could be used only in respect of the assessment year to which it

related and that on the basis of a document which related to a particular year, the expenditure of other assessment years could not be estimated. Apart from this legal contention, the assessee also contended that while estimating the household expenditure, the AO had ignored the withdrawals made by his wife and his mother who were living with him and the fact that the expenditure in regard to visits to Dubai were borne by his brother Purushottam Khatri.

7. On the other hand, the Revenue contended that the AO was entitled to estimate the expenditure during the entire block period on the basis of any document seized during the course of search if the assessee did not come forward with a satisfactory explanation. It was submitted that having regard to the provisions of Section 158BB, the total income of the entire block period has to be determined as per provisions of Chapter IV, on the basis of evidence found as a result of search u/s 132 and such other materials or information as are available with the AO and the income assessed therefrom or shown in the returns of the relevant assessment years falling in the block period filed prior to the date of search is to be excluded to arrive at the undisclosed income of the block period. It was contended that the interpretation that in a block assessment, the loans, assets, investments or expenditure which are already shown in the returns of the relevant assessment years falling in the block period filed prior to the date of search, cannot be inquired into, is incorrect. It was submitted that such an interpretation was against the express provisions of Section 158BB which prescribed the manner of computation of undisclosed income for the block period. It was pointed out that if such inquiries are not made in the block assessment proceedings, the assessments of the relevant assessment years will have to be reopened u/s 147 which will lead to multiplicity of proceedings for different assessment years falling in the block period, which definitely was not the intention of legislature in enacting the special provisions in Chapter XIV-B for expeditious disposal of such assessments.

8. The Tribunal, after examining the seized documents, held that the loose slip related to the year in which the search had taken place (year ending 31st March, 1.997) and did not relate to other years in the block period. The Tribunal held that proceedings relating to regular assessment and block assessment are distinct and different and that while regular assessment u/s 143(3) is to be framed on the basis of the return of income filed by the assessee before the AO, block assessment is framed on the basis of material seized during the course of search; that, having regard to the definition in Section 158B(b) of the Act, "undisclosed income" is only that income which has not been or would not have been disclosed for purposes of the Act and the income declared in the return of income cannot be termed as undisclosed income for the purpose of Chapter XIV-B. The Tribunal held that the block assessment of undisclosed income should be computed as per the procedure laid down u/s 158BB and due credit of the income declared and the claim raised in the regular return of income should be given by the AO. The Tribunal further held that in block assessment, the AO should compute the undisclosed income on the basis of documents and material

seized during the course of search. Where the assessee had claimed withdrawal of household expenses every year while computing the total income and that has been accepted by the AO, the same cannot be reopened or examined by the AO while framing the block assessment, on the basis of seized documents, which do not relate to that assessment year. The Tribunal further held that the seized documents, at best, can be used to estimate the household expenses for that assessment year to which it relates, but, while doing so, the AO should have given due credit for the household expenses claimed by the assessee. The Tribunal also held that the AO ought to have examined the details of withdrawals made by the family members of the assessee (and used towards household expenses) and given a finding thereon. As a consequence of its conclusion that the seized documents cannot be used for estimating the household expenses of other assessment years for which returns were filed by the assessee in time claiming the household expenses, the Tribunal directed the AO to delete the addition on account of household expenses estimated for the asst. yrs. 1988-89 to 1996-97. Insofar as the asst. yr. 1997-98 is concerned, the Tribunal directed the AO to re-examine the household expenditure with reference to withdrawals made by other family members and the certificate of Purushottam Khatri in regard to travelling expenses of the assessee.

9. Sub-section (1) of Section 158BA of the Act provides that notwithstanding anything contained in any other provisions of the Act, where, after the 30th day of June, 1995, a search is initiated u/s 132 (or books of account, other documents or any assets are requisitioned u/s 132A) in the case of any person, then, the AO shall proceed to assess the undisclosed income in accordance with the provisions of Chapter XIV-B. Sub-section (2) of Section 158BA reads thus :

Sub-section (2) : "The total undisclosed income relating to the block period shall be charged to tax, at the rate specified in Section 113, as income of the block period irrespective of the previous year or years to which such income relates and irrespective of the fact whether regular assessment for any one or more of the relevant assessment years is pending or not.

Explanation.--For the removal of doubts, it is hereby declared that--

- (a) the assessment made under this Chapter shall be in addition to the regular assessment in respect of each previous year included in the block period;
- (b) the total undisclosed income relating to the block period shall not include the income assessed in any regular assessment as income of such block period;
- (c) the income assessed in this Chapter shall not be included in the regular assessment of any previous year included in the block period."

The term "undisclosed income" was defined thus in Section 158B(b) at the time when the AO made the block assessment on 29th Oct., 1997 and when the Tribunal decided the appeal on 21st May, 2001 ;

Section 158B(b) : "'undisclosed income" includes any money, bullion, jewellery

or other valuable article or thing or any income based on any entry in the books of accounts or other documents or transactions, where such money, bullion, jewellery, valuable article, thing, entry in the books of account or other documents or transaction represents wholly or partly income or property which has not been or would not have been disclosed for the purposes of this Act."

Subsequently, by finance Act, 2002, the following words were added with retrospective effect from 1st July, 1995, at the end of the above definition of "undisclosed income" u/s 158B(b) :

"Or any expense, deduction or allowance claimed under this Act which is found to be false."

10. The effect of the said amendment is clarified as follows in the Explanatory Note on provisions relating to direct taxes contained in the CBDT Circular No. 8 of 2002, dt. 27th Aug., :

"61.2 : The existing provisions of Clause (b) of Section 158B define "undisclosed income" to include income or property which has not been or would not have been disclosed for the purposes of this Act, and which is represented by any money, bullion, jewellery or other valuable article or thing, or by any entry in the books of accounts or other document or any other transaction. It has been noticed that in some cases the appellate authorities have taken a view that the definition covers only property or receipts which have not been disclosed and does not cover income represented by entries in respect of false claims of expenses or deductions. Such view is contrary to the intention underlying the provision of bringing to tax the entire undisclosed income, including income which has been suppressed by making false claims of expenses or deduction, which have been discovered as a result of search or requisition....

61.3.2 : The Finance Act, 2002, has amended Section 158BB to clarify that the block assessment of undisclosed income is to be based on the evidence found in the search and material or information gathered in post-search inquiries made on the basis of evidence found in the search."

11. The effect of the amendment to the definition of "undisclosed income", therefore, is that any income which has been suppressed by making any false claims of expenditure or deduction or allowance, discovered as a result of search or requisition could be added as undisclosed income. A false claim of expenses or deduction can be of two types. First will be where the assessee gives a bloated figure of expenditure or deduction so as to reduce the assessable income and subsequently, it is found that the claim of expenditure or deduction is false, that is much less than what was claimed. The second type is where the assessee shows a much lesser expenditure so as to fall within the income declared and subsequently, it is found that the expenditure incurred was much more which would mean that the income was much more than what was declared as income. The case on hand falls under the second category, which may be clarified by an example. An assessee manufactures a product at a cost of Rs. 60,000 per unit,

sells it at Rs. 85,000 per unit and shows a trade discount of Rs. 20,000 per unit, and profit as Rs. 5,000 per unit. Subsequently, it is found that he had given only a trade discount of only Rs. 2,000 per unit and not Rs. 20,000. The difference of Rs. 18,000 per unit will have to be added as "undisclosed income". This is the first type of false claim of expense/deduction/ allowance. A person shows the net income in a year as Rs. one lac and shows the household expenditure as Rs. 5,000 per month or Rs. 60,000 per year which is well within the net income. Subsequently, during a search, it is found that the actual household expenditure was Rs. 15,000 per month or Rs. 1,80,000 per year. The assessee is not in a position to explain the source of funds for such expenditure in excess of the known sources of funds/income. Necessarily, it has to be implied that the lesser household expenditure that was shown was false, that the income was much more and the unexplained part of household expenditure will have to be added as undisclosed income. This is the second type of fake expense/deduction/ allowance. Both would fall under "any expense which is found to be false" occurring in Section 158B(b). Therefore, where the search discloses any expenditure which is found to be false, appropriate additions can be made but what is relevant is the addition can be made only in regard to the income related to false claim of expenditure disclosed by the material unearthed during the search.

12. Coming to the facts of this case, the only document that was found with reference to household expenditure is loose slip No. 7 which did not bear any date. It also did not state as to which period it related to. It merely gave details of household expenditure totalling to Rs. 14,000. In the absence of any indication as to which month or year to which it related, the AO proceeded on the basis that it related to a monthly expense during the year in which search was made and the document was found, that is asst. yr. 1997-98. He also proceeded on the basis that there would have been similar monthly household expense during the year, in the absence of any explanation of special expenses during the particular month. This is not open to challenge. From one incident of suppression in an accounting year, relating to periodical recurring expenditure, the AO was logically entitled to infer that there were other similar suppressions of expenditure during the entire assessment year, in the absence of any special features [vide *The Commissioner of Sales Tax, Madhya Pradesh Vs. H.M. Esufali, H.M. Abdulali, Siyaganj, Main Road, Indore, and Bhimraj Pannalal Vs. Commissioner of Income Tax, Bihar and Orissa*,]. But as the AO had not considered the contention of the assessee that the withdrawals made by other family members (wife and mother) during the year should be considered as sources for household expenditure, though material was produced in support of the contention, the Tribunal has rightly directed the AO to give due credit for the same for the asst. yr. 1997-98.

13. The next question is whether the AO was justified in proceeding on the basis that the household expenses which was Rs. 14,000 per month during the accounting year 1996-97 would have been the same during the earlier 10 years

and treating the said expenditure (that is 14,000 x 12 subject to a deduction of 10 per cent per year due to inflation) as the household expenditure and adding the same as undisclosed income. This did not rightly find favour with the Tribunal. There is absolutely no basis for assuming that the expenditure incurred during a particular month/year should be the expenditure during the previous 10 years also. The monthly household expenditure may depend on various circumstances. One important factor is the earning/income. There may also be sudden variations in the monthly household expenditure, having regard to cost of education, treatment of illness, travelling, etc. Except for such spurts in expenditure, normally household expenditure would depend upon the income. For example, if the monthly income was Rs. 5,000 during the first year, the expenditure is likely to be Rs. 4,000 per month; if the income was Rs. 10,000 per month during the second year, the expenditure is likely to be Rs. 8,000 per month; if the income was Rs. 15,000 during the third year, the expenditure is likely to be Rs. 12,000 per month; and if the income was Rs. 20,000 per month, during the fourth year, the expenditure is likely to be Rs. 16,000. In other words, there is a normal tendency to spend more in proportion to the rise in income. But if the income is limited, the tendency is to limit the expenditure. Therefore, there is no logic in saying that a person who spent Rs. 16,000 in a month during the fourth year (when his income was Rs. 20,000 per month), would have spent the same sum of Rs. 16,000 per month during the first year also (subject to correction on account of inflation) when the income was hardly Rs. 5,000 per month. In matters relating to household expenditure, where normally the monthly expenditure tend to depend upon the income, it is not permissible to assess the expenditure during previous years with reference to the expenditure during a later year (when income was more).

14. While there can be no hard and fast rule as to the material on which income could be estimated, it can definitely be said that estimating the household expenditure in a particular year, with reference to the income of a future year (that too 5 to 10 years later) in the absence of any other evidence, would be arbitrary and illogical. In fact the income of the assessee determined by the AO excluding the addition made as unexplained household expenditure, when compared to the amount added as household expenditure, would demonstrate this position. We extract the relevant figures below :

Assessment Income computed by Amount added as Year AO after additions unexplained household (other than household expenditure on the basis of expenditure) household expenses (Rs.) determined for the asst. yr. 1997-98 (Rs.) 1987-88 44,494 66,640 1988-89 53,330 73,720 1989-90 80,768 73,150 1990-91 30,300 86,560 1991-92 39,210 1,03,930 1992-93 64,380 1,03,980 1993-94 1,64,525 1,14,170 1994-95 86,710 1,06,260 1995-96 1,05,110 1,33,980 1996-97 1,40,640 1,42,200 It will be seen that the figures of household expenditure (added by the AO) appear to be wholly disproportionate to the income. The above figures demonstrate that the household expense determined for a particular month in a later year (asst. yr. 1997-98), cannot be

the basis for determining the monthly household expenditure during years when the income was considerably low.

15. The Tribunal, therefore, has rightly held that in the absence of any material to show that there was a higher household expenditure (than disclosed while filing returns) during the previous assessment years, the AO was not justified in estimating the household expenditure for the previous years by taking Rs. 14,000 (expenditure during 1997-98) as the base figure. The Tribunal has rightly restricted the use of the slip containing the details of the household expenditure to the year during which it has been found and rightly deleted the additions under the head of "unexplained (household) expenditure". We, therefore, answer question No. (ii) in the affirmative and against the Revenue.

Re. Question (i):

16. The Tribunal has not held that the income disclosed in the return for the relevant assessment year could not be investigated in the block assessment u/s 158BC. Section 158BB of the Act provides that for computing the undisclosed income of the block period, the total income determined on the basis of assessments under Sections 143, 144 and 147 (or where the returns of income have been filed but the assessments have not been made till the date the search, the income disclosed in such returns) will have to be excluded from the aggregate of total income of the previous years falling within the block periods. The Tribunal held :

"Since the issue with regard to the household expenses has been properly adjudicated in the regular assessment of different assessment years of the block period, the same cannot be reopened or examined by the AO while framing the block assessment on the basis of the seized documents which do not relate to the assessment year. At the most, the seized document can be used to estimate the household expenses only for that assessment year to which it relates...."

(Emphasis, italicised in print, supplied)

The above observations should be understood in the context of household expenses disclosed for a particular month during the year of search. Having stated as above, the Tribunal also observed--

"The issue relating to the particular claim which has been raised by the assessee in the regular return of income and that return was duly assessed by the AO, should not be reopened or re-examined by the AO while framing the block assessment of the assessee."

17. The above observation of the Tribunal should be understood in the context in which it was made. What the Tribunal meant was that where the assessee had disclosed the withdrawals of household expenses while computing the income and that has been accepted by the AO, it cannot be reopened while framing block assessment, in the absence of any material to suspect or conclude that though the household expenses were higher, a lesser expense was shown. If para 14 of

the Tribunal's order is read in entirety, it is evident that the Tribunal did not lay down any proposition that a "matter" disclosed in the return for the relevant assessment year could not be investigated in the block assessment u/s 158BC. Therefore, question (i) does not arise for consideration.

18. In view of the above, the appeal is dismissed.