

(2000) 02 KL CK 0062

In the High Court Of Kerala

Case No : IT Ref. No. 36 of 1997 28 February 2000 A.Y. 1989-90

COMMISSIONER OF INCOME TAX

APPELLANT

Vs

K. N. SATYAPALAN

RESPONDENT

Date of Decision : 28-02-2000

Acts Referred:

Income Tax Act, 1961 — Section 256

Citation : (2000) 110 TAXMAN 151

Hon'ble Judges : Arijit Pasayat, C.J;K. S. Radhakrishnan, J

Bench : Full Bench

Advocate : P. K. R. Menon, for the Revenue C. Kochunny Nair, K.G. Anil Babu and S. Arun Raj, for the Assessee, for the Appellant;

Judgement

Arijit Pasayat, CJ.

Pursuant to direction given by this court in O.P. No. 11914 of 1994 dated 7-11-1994, following questions have been referred for the opinion of this court u/s 256(2) of Income Tax Act, 1961 (hereinafter referred to as "the Act") by the Tribunal, Cochin Bench.

1. Whether, the Tribunal was justified on the facts and in the circumstances of the case in deleting the addition of Rs. 22,26,538?

2. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law and on facts to hold that the assessee had utilised the secret profits of the firm for his proprietary business?

2. Factual position, as stated in the statement of case, is as follows: The assessee is a partner in the firm, K. N. Sathyapalan & Co., which was carrying on contract business. He was also doing independent contract work on a proprietary basis. During accounting year ending on 31-3-1989 relevant to the assessment year 1989-90, the assessee had undertaken contract work in respect of Chimini Dam and Kanjirapuzha Dam. In respect of these works, he had disclosed gross receipts of Rs. 99,73,121, which included value of materials supplied by State

Public Works Department for a sum of Rs. 25,50,068. The assessing officer determined total income at Rs. 48,96,660, which included addition of Rs. 22,26,538 as income by way of unexplained investment. Reason for such addition was that the assessee had made certain deposits and advances and incurred expenditure, the sum total of which comes to Rs. 30,15,050. The assessee was able to explain the sources only to the extent of Rs. 7,10,300 and balance was treated as unexplained investments. The assessee preferred an appeal before the Commissioner (Appeals), Trivandrum, who sustained the addition. Matter was taken in appeal before the Tribunal by the assessee. The Tribunal deleted the addition by holding that income disclosed by the firm before the Settlement Commission was available to be utilised by the assessee. Reliance was placed on the decision of Apex court in *Anantharam Veerasinghaiah and Co. Vs. Commissioner of Income Tax , Andhra Pradesh*, to hold that funds siphoned off from the firm were available with assessee for explaining the investments in his books for the previous year ending on 31-3-1989. The revenue prayed for reference to this court, which was rejected. But, pursuant to the direction given as indicated above, questions as quoted above have been referred for opinion.

3. In Support of the application, the learned counsel for the revenue submitted that the Tribunal lost sight of the actual background of the facts and proceeded to base its conclusions on surmises and conjectures. Reference was made to the balance sheets which were available before the Settlement Commission. After disclosure, it was noticed that credit balances of all the partners excepting S/Shri K.N. Sathyapalan and K.N. Mohanan were in the liability side along with creditors for materials. Position was completely transformed after the disclosure made to the Settlement Commission. By the end of 31-3-1987, credit balance of all the partners excepting Shri Sathyapalan had correspondingly increased. Two items of creditors for materials and wages payable were deleted as was noticed by the Commissioner (Appeals). Revised balance-sheet was possible to be prepared only after the firm had filed petition before the Settlement Commission, or only after the Settlement Commission gave their order on 21-2-1991. If that is so, the revised balance sheet is only a readjustment of credit and debit balances of various partners. An amount of Rs. 31,75,000 was reduced only in respect of creditors for materials and wages payable. Therefore, question of availability of cash in the books of accounts does not arise, as there is no change in respect of assets mentioned in the balance sheet.

4. According to the learned counsel for the assessee, conclusions of Tribunal are factual giving rise to no question of law. It clearly held that there was availability of funds flowing from the settlements made in respect of the firm, and settled amount was utilised by the assessee only.

5. A few factual aspects, which have relevance, need to be noted. It is true, as contended by the learned counsel for the assessee, if factual conclusions are arrived at by the Tribunal, which is final fact-finding authority, no question of law would arise consideration. But, if the Tribunal takes into account irrelevant

materials or leaves out of consideration relevant materials, conclusions will be vitiated giving rise to question of law. It has to be noted that the assessee accepted certain factual aspects.

These are relatable to settlement made in case of the firm. Bogus entries in relation to expenses were made thereby reducing profits. Correspondingly, bogus entries were made in respect of alleged creditors. After settlement, what was done was to reverse the entries relating to alleged creditors vis-a-vis corresponding bogus entries in respect of expenses. Net effect of such reversal of entries was deletion of entries from balance-sheet, profit and loss account, and corresponding increase in capital account of partners of the firm. This did not lead to generation of cash inflow into the firm. Consequently, there was no question of any outgoing from the corpus of firm to the hands of assessee. Additionally, the Tribunal seems to have lost sight of the fact that if a sum of Rs. 22 lakhs was available as cash, the assessee and the firm would not have obtained over-draft facility of more than Rs. 25 lakhs from banks. Right from assessment year 1986-87 onwards, cash credit from various parties aggregating to Rs. 28 lakhs was claimed by the assessee. As has been rightly observed by the assessing officer and first appellate authority, there was no co-relation between withdrawals made on various dates. In fact, small amounts were withdrawn on various dates. The Tribunal was of the view that when inflated wages and materials were shown by setting up bogus creditors, it meant that inflated liabilities are paid off in the course of year or in subsequent year and in the cash book, cash which is obtained through receipts is reduced and, thus, the money is siphoned off from the firm and this is possible because of generation of funds. Such conclusion, to say the least, is erroneous and confusing. Procedure adopted by the firm was, as contended by the assessee, to show bogus expenses by inflation of wages and materials. It was not the case of assessee, at any stage, that expenses were, in fact, made from undisclosed sources and they were not reflected in the accounts. That being the case, there would not have been any generation of cash. It is also not the case of the assessee that by showing bogus expenditure, firm was keeping the money to itself. Admitted fact being that firm was inflating expenses and showing bogus credits but actually no cash is involved in the transaction. By reversal of entries, effect of credits and debits was neutralized. There was no question of generation of any cash as contended by the assessee and accepted by the Tribunal. Position would not have also been different had actually expenses been made from undisclosed sources, against which bogus entries of creditors had been made. In such a case also, cash would have also been spent and no longer available. Case at hand, as noted above is one of inflation of expenses when in fact no expenses were made. To explain the expenses, entries in respect of bogus creditors were made. Had it been a case of bogus expenditure without actual payment, to reduce profit, cash would have been available. That is because without cash being spent out of funds available, it is claimed to have been spent. Consequently, the conclusion of the Tribunal about availability of cash is clearly untenable. Merely because secret

profits were made by firm as claimed, that was not relatable to existence of cash. Another plea that was raised was that the Tribunal brushed aside the factual aspect regarding discharge of liability in respect of purchase of 178.58 acres of estate for Rs. 15 lakhs. Long after the completion of assessment, a revised return was filed admitting a further surm of Rs. 7,01,550 as additional income. This was held to be not of much consequence by the Tribunal on ground that the assessee was not expected to be a paragon of virtues. In the purported revised return, it was stated that loans were raised by two persons who were incharge of the execution of work, and such funds were in the savings bank account of respective persons. We find that the Tribunal did not attach much importance to the question whether the other 13 partners had a share in profits and whether the amount was distributed. It was for the assessee to establish that there was no distribution among other partners, which it failed to do. These aspects are really not of any importance in view of our conclusion that no cash was available to be invested. The Tribunal acted on irrelevant materials, leaving out of consideration relevant materials and, therefore, its order is vitiated. Its conclusions are not supportable on the basis of materials on record.

Our answer to both the questions referred to above is in the negative, in favour of revenue and against the assessee.