
(1974) 11 PAT CK 0012
In the Patna High Court
Case No : Tax Case No. 78 of 1970

Md. Umer

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

Date of Decision : 18-11-1974

Acts Referred:

Income Tax Act, 1961 — Section 254, 256(1), 256(2)

Citation : (1975) 101 ITR 525

Hon'ble Judges : S.N.P. Singh, C.J;S.K. Jha, J

Bench : Division Bench

Advocate : K.N. Jain and G.C. Bharuka, for the Appellant; Shambu Sharan, for the Respondent

Judgement

S.K. Jha, J.—In pursuance of a direction of this court u/s 256(2) of the Income Tax Act, 1961 (hereinafter referred to as "the Act"), two questions of law have been referred for the opinion of this court by the Income Tax Appellate Tribunal, Patna Bench. They are as follows :

"(1) Whether, in the facts and circumstances of the case, the finding of the Tribunal upholding the rejection of the book profit shown by the assessee, is not vitiated by reason of its reliance upon suspicion, surmises as also on irrelevant material.?"

(2) Whether, in the facts and circumstances of the case, the finding given by the Tribunal that the sales made by the assessee during the relevant year were unverifiable is based on record or is an arbitrary finding?"

2. The short facts relevant for the disposal of this reference may be summed up thus. The assessee is an individual who derives income from the sale of country liquor. The assessment year with which we are concerned in this reference is 1966-67, for which the assessee filed a return showing a total turnover on account of the sales in the course of the year in question at Rs. 12,90,678 and a net profit of Rs. 22,218, which came to about 1.75 per cent. The books of

account were duly produced by the assessee and his representative, and the Income Tax Officer found, on examination of the account books, three defects relating thereto : (1) that the sales were not verifiable in the absence of cash memos, (2) that they were noted in lump sums, and (3) that the drawings of personal expenses shown by the assessee during the year at Rs. 3,176 seemed to be inadequate. The Income Tax Officer further held that the assessee had no agricultural income. In these circumstances, the book profits shown by the assessee were not accepted and his sales were estimated at Rs. 12,95,000, and a flat rate of 2"5 per cent. on net profit of Rs. 29,875 was assessed, A copy of the order of the Income Tax Officer has been marked annexure "A" to the statement of the case. The assessee preferred an appeal before the Appellate Assistant Commissioner who also held that for the reasons discussed in the assessment order, the "book profits" shown could not be accepted as correct. A copy of the appellate order forms part of the statement of the case as annexure "B". The assessee having preferred a second appeal to the Tribunal contended that the rejection of the book results of the assessee and estimation of profit by resorting to the proviso to Section 145(1) of the Act was wholly unwarranted, both on the facts and in the circumstances of the case as well as in law. It was urged on behalf of the assessee that the sales were verifiable, inasmuch as complete data regarding purchases, sales, opening and closing stocks were available. The sale price of country liquor was fixed by the excise department of the Government, and the sales could not, therefore, be more than what had been shown by the assessee. It was further contended that the sale of the quantity of liquor as furnished by the assessee could be further verified with reference to the purchase and the stock at the moment as the commodity was rationalised by the excise authorities. None of the arguments on behalf of the assessee, however, found favour with the Tribunal which referred to the assessee's appeal in respect of the previous year and held that the defects as pointed out in the earlier year still being there, the revenue authorities were well justified in rejecting the "books results" and estimating the net profits as well as in enhancing the flat rate. The assessee's appeal was accordingly dismissed.

3. The assessee, thereafter, filed an application u/s 254 of the Act for rectification of a mistake which was rejected by an order dated the 4th of February, 1971. Copies of the orders of the Tribunal for the assessment years 1963-64 and 1966-67 and the order u/s 254 as earlier mentioned form part of the statement of the case marked annexure "C" series. An application u/s 256(1) of the Act having been rejected by the Tribunal, this court directed the Tribunal to refer to it the aforesaid two questions of law.

4. From annexure "C-II" forming part of the statement of the case which is an order u/s 254 of the Act, it appears that during the previous year five reasons had been recorded by the Tribunal for rejecting the book profits of the assessee for that year. They have been enumerated by the Tribunal as follows :

"(1) The sales were not verifiable.

(2) From the point of drawing of the liquor from the barrels, no account was maintained and even the normal leakage in the process of drawing and filling in the bottles was not shown.

(3) Year to year the book results shown have been rejected and profit invariably estimated by the department.

(4) The percentage of profit shown was low.

(5) Drawings for expenses were inadequate."

5. As has already been noticed above, the assessee had produced all his books of account before the Income Tax Officer, which had been duly examined by him and the defects as pointed out by the Tribunal with regard to a previous year were not all found by the Income Tax Officer. The only two defects found by the Income Tax Officer, for rejecting the book profits or the trading results were that in the absence of cash memos, the sales were not verifiable and that certain transactions were noted in lump sums. No finding has been recorded by either of the authorities below as to the unacceptability of the method and irregularity of the account kept by the assessee. It is well-settled that in the absence of such a finding recorded by the authorities, the book results cannot be ignored or brushed aside. As has been held by a Bench of the Bombay High Court in *R.B. Bansilal Abirchand Spinning and Weaving Mills Vs. Commissioner of Income Tax, Poona*, the mere fact that the percentage of dead loss of cotton is high in a particular year cannot lead to an inference that thereby there has been a suppression of the production in the spinning mill. So also in the case of *R.B. Jessaram Fetechand (Sugar Dept.) Vs. Commissioner of Income Tax, Bombay City-II*, where the trading results had been rejected by the revenue on considerations not germane to the unacceptability of either the regularity or the mode of account maintained, additions by way of estimate were struck down. Since at one stage learned counsel on behalf of the department vehemently contended that the order of the Tribunal or for that matter the order of the revenue authorities below should not be treated to be one under the proviso to Section 145(1), but as being an order u/s 145(2). I must point out that this has never been the stand of the department at any stage of the proceedings. All the authorities below including the Tribunal have resorted to the provisions of the proviso to Sub-section (1) of Section 145. At all stages what has been done by the revenue is to have rejected the trading results or the book profits; the entries in the books of account had nowhere been found to be either unacceptable or untrue. The finding of the Tribunal that the defects which had been pointed out by it with regard to the assessment of the previous year of this assessee were still there, is clearly an error of record which, in my view, is a question of law. Out of the five defects pointed out by the Tribunal in the previous year's assessment proceedings, the Income Tax Officer has recorded only two defects, if at all they can be termed as defects, namely, the absence of the verifiability of the account, the cash memos not being preserved, and the low figure of the drawings of personal expenses. The Tribunal, therefore, was in

serious error in holding that the assessee's books of account for the relevant year with which we are concerned suffer from the same infirmities as the account books of the previous years. As has already been noticed from the recital in the statement of the case submitted by the Tribunal, it has all along been the case of the assessee that the sales were verifiable inasmuch as complete data with regard to the purchases, sales, opening and closing stocks were available. The assessee has also been crying hoarse that since the commodity in question in which the assessee was dealing was in direct control of the excise department of the Government and was a rationalised commodity, there could be absolutely no difficulty in having the amount of liquor sold verified from the excise department. The rules under the excise law enjoin the department concerned to fix the sale price and, therefore, no assessee can charge any more sale price than what has been fixed by the department. There was absolutely no reason not to have accepted the explanation of the assessee that the figures in the records of the excise department could very well show the genuineness or otherwise of the entries of the assessee's books of account. Be that as it may, as I have already stated above, it is not a case of rejection of the assessee's books of account u/s 145(2) of the Act. It is a case under the provisions of the proviso to Sub-section (1) of Section 145. And it is well nigh settled that in any case where the accounts are correct and complete but the method employed is such that the income, profits and gains cannot properly be deduced therefrom, the Income Tax Officer is bound under this proviso to compute the income upon the basis and in a manner to be determined by himself. u/s 13 of the Indian Income Tax Act, 1922, the corresponding proviso applied with equal force both to the provisions u/s 145(1) and u/s 145(2) of the 1961 Act. But such is no longer the position. The case, proviso to Section 13 of the 1922 Act, has now been made applicable and that too only partially to the provisions of Sub-section (1) of Section 145. And while taking resort to the provision of this proviso, the Income Tax Officer must give a definite finding that the case falls within the proviso. As held by the Supreme Court in the case of *The Commissioner of Income Tax, Madras Vs. A. Krishnaswami Mudaliar and Others*, , this proviso (while their Lordships were considering the effect and scope of Section 13 of the 1922 Act) imposes a statutory duty on the Income Tax Officer to examine in every case the method of accounting employed by the assessee and to see whether or not it has been regularly employed and to determine whether the income, profits and gains of the assessee could properly be deduced therefrom. Once, therefore, the method of accounting employed by the assessee has been regularly employed and income, profits and gains could properly be deduced from such regularly employed method of accounting, that is the end of the matter for the purpose of the proviso to Sub-section (1) of Section 145. As has already been held above, there is no finding in the present case that any of the entries in the books of account was not correct, there is no finding that the assessee is not employing a method of accounting and there is no finding that such a method of accounting has been irregularly employed by the assessee. In the absence of any such finding, there being no reason germane to the unacceptability of the book

results, it must be held that the Tribunal as well as the revenue authorities below had no materials before them, on the basis of which it could be said that the trading results were not verifiable and that, therefore, they should not be accepted, nor is it their case that the trading results could not be deducible from the entries of the books of account regularly employed.

6. As has been held in the case of C. Arumugaswami Nadar Vs. Commissioner of Income Tax, Madras, , if there is no material before the Income Tax Officer to justify the finding that income cannot be properly deduced from the assessee's regular method of accounting, the assessment made in pursuance of this proviso would be vitiated.

7. For the reasons stated above, I must answer both the questions in favour of the assessee and against the department and hold that on the facts and in the circumstances of the case the finding of the Tribunal upholding the rejection of the book profit shown by the assessee was vitiated by reason of its reliance upon suspicion, surmises as also irrelevant material. I also hold in the circumstances of the case that the finding given by the Tribunal that the sales made by the assessee during the relevant year were unverifiable is not based on the materials on record and is an arbitrary finding. The assessee will be entitled to the costs of this reference.

8. Hearing fee Rs. 100 only.

S.N.P. Singh, C.J.

9. I agree.