

Vijay Raj Sethia Vs. Asstt. Cit

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Court : Income Tax Appellate Tribunal ITAT Hyderabad

Decided On : Feb-27-2006

Judge : N Raghavan, Vice, J S Reddy

Appellant : Vijay Raj Sethia

Respondent : Asstt. Cit

Judgement :

1. These appeals, two by assessees and two by the revenue, are directed against separate but identical orders of the Commissioner (Appeals) 1, Hyderabad, dated 23-6-2003 in the case of Vijay Raj Sethiya and dated 30-6-2003 in the case of Uttam Chand Sethiya, for block assessment period 1991-92 to 2001-02 and up to 23-11-2001. As the issues arising in these appeals are common, for the sake of convenience, these appeals were heard together and are disposed of by a common order. Brief facts are as follows.

2. The assessees were carrying on clandestine business in purchase and sale of N-Hexane, a solvent product used in pharmaceuticals. The modus operandi of this activity is that since there is no perceptible difference between Hexane products and Petroleum ether, the same was being sold to petroleum bunks for adulteration ie. mixing it with petrol. Taking advantage of the explosive licence and certification from Industries department as regards storage capacity which the assessee had, the assessee used to purchase the solvent oil from oil companies, lift the stocks and sell the same in open market for profit by the clandestine activity. The oil companies, which are public sector undertakings, in order to control adulteration, had stopped bulk sale of this product and were instead supplying to individual purchasers.

Since the purchase of the said chemical could be made in small quantities, that too by making payment by means of demand draft only, a bank account was opened in the individual name of the assessee exclusively for this activity. A search and seizure operation was conducted under Section 132 on 23-11-2000. During the search, a bank account held by the assessee was seized. The transactions recorded in the bank account did not form part of regular books of account maintained by the assessee. In a statement under Section 132(4), the assessee agreed that the said bank account was operated exclusively for the purposes of the above mentioned activity and that he used to obtain monies from prospective purchases of the chemical, deposit the same in the said account, obtain DDs from the said account in favour of suppliers, lift the stock from them and then sell the same in the open market. The assessees filed block returns in response to notice under Section 158BC issued on 31-5-2001.

3. In the block return, Shri Vijay Raj Sethiya admitted undisclosed income for the block period at Rs. 10,81,000, the break-up of which is as follows: 4. Shri Uttam Chand Sethiya declared an income of Rs. 5,46,000 from this activity. The assessing officer estimated the margin of profit on this illegal activity at 15% on estimated purchase turnover of Rs. 1,46,45,863 in the case of Shri Vijay Raj Sethiya. In the case of Shri Uttam Chand Sethiya, he estimated the profit at 1596 from undisclosed business activity of trading in N-Hexane at Rs. 10,73,298. The assessees carried the matter in appeal. The first appellate authority held that in illegal business, the margin of profit would be less as a customer would pay less price if he was to know that the commodity is sold outside the regular books of account, to avoid payment of tax to Government. He further

observed that the assessing officer had accepted profit percentage of 8.2596 in similar line of business in the case of Shri P. Koteswara Rao, who was also covered under the search operation under Section 132 on 23-11-2000. Thus, he directed the assessing officer to apply a rate of 8.2596 gross profit. Aggrieved of these directions, both the assessee and the revenue are in appeal.

One additional point that arises for our consideration in the case of hri Uttam Chand Sethiya is the claim for telescoping. The assessee claims that the income derived from undisclosed business activity should be telescoped and no separate addition should be made on account of undisclosed assets. His case is that the claim of the assessee that Rs. 3,23,710, being cash related to three business concerns, was accepted by the revenue and the balance of Rs. 4,08,125 should be held as cash generated from undisclosed business and not brought to tax separately.

5. The learned Counsel for the assessee reiterated his submissions made before the first appellate authority. He filed a paper book running into 38 pages in the case of Vijay Raj Sethiya and 33 pages in the case of Uttam Chand Sethiya. The main contentions of the assessee can be summarised as follows :? (1) The assessing officer erred in estimating the sales at cost price plus 5% and in turn estimating a further 1596 on the sales so determined for bringing to tax, as the same is an arbitrary method 'without any basis. J.' (2) As authentic sale figures are not available, working out of profit at 596 of purchases, which is adopted by the assessee, should have been upheld. (4) The Commissioner (Appeals) was wrong in taking the case of Shri P. Koteswara Rao as a comparable case, for the reason that in the case of Shri Koteswara Rao, the product in question, ie. N-Hexane, was sold under a changed name as Petroleum Ether and this might have resulted in a higher profit. A sister concern of the assessee, viz., Sayar Chemical Industries, disclosed profit of less than 596 and this was accepted by the department.

(5) The Commercial Taxes Officer, Marredpally Circle, has estimated the profit at 1096 of total purchases.

(6) A sale outside the books of account would result in lesser amount of profit as compared to sale made officially.

6. In the case of Shri Uttam Chand Sethiya, in addition to the above submissions, the learned Counsel for the assessee submitted that the undisclosed business definitely gives rise to certain income and this income would manifest itself in the form of assets and as Rs. 5,46,000 had already been admitted by the assessee, no separate addition is called for on account of cash generated out of undisclosed business.

For the proposition that telescoping has to be granted, he relied on the following case laws :? 7. The learned departmental representative, on the other hand, vehemently controverted the arguments of the learned Counsel for the assessee and submitted that the proposition being advanced by the assessee and accepted by the first appellate authority is contrary to facts and probabilities in this case. She submitted that the assessee had admittedly indulged in an illegal business which makes him liable to prosecution and severe punishments and penalties. She wondered as to how a view could be taken that when an assessee takes such great risks, his profits would be less than an assessee who does the business in a law-abiding manner. She submitted that just to derive higher margins of profit the assessee had indulged in this business of adulteration.

8. As regards the direction of the Commissioner (Appeals) in the case of Shri P. Koteswara Rao to the assessing officer to accept a percentage of 8.596, she submitted that Shri P. Koteswara Rao was only a commission agent whereas the assessee here were doing business in this particular product. She vehemently contended that when the percentage of profit in the case of a commission agent is 8 ' 2596, the percentage of profit derived by the assessee, who is in the business of trading in his product, would be much higher, especially when he has also paid certain commission to Shri Koteswara Rao. She submitted that the assessing officer had adopted a fair method in this case. As the assessee did not have any account of sales, the only basis available was to take the purchases as per bank account and estimate sales at cost plus 5 96 and thereafter determine the profit at 1596 on such sales. She strongly submitted that the Commissioner (Appeals) has wrongly given relief to the assessee and that the orders of the Commissioner (Appeals) to that

extent have to be vacated and the orders of the assessing officer restored.

9. On the issue of telescoping, the learned departmental representative submitted that in all the case laws cited by the learned Counsel for the assessee, a nexus, between the undisclosed income and the assets purchased had been shown, whereas in this case the entire amounts were in the bank account, in the sense that the receipts from unaccounted sales were deposited in the bank account for the purpose of obtaining DDs in favour of public sector oil companies. She contended that unless some drawings are shown from the bank account, the question of telescoping would not arise as there would be no nexus whatever between the undisclosed income and the case found during the course of search.

10. Joining the issue, the learned Counsel for the assessee submitted that at page 13 of his paper book, the break-up of undisclosed income of Shri P. Koteswara Rao is given and in that it is shown that sale of 55 tankers of Petroleum Ether had been undertaken by Shri Koteswara Rao. He pointed out that the assessing officer in that case, where Shri Koteswara Rao acted as a businessman, had accepted the gross profit rate of 8.2596. He also pointed out that the commission received at Rs. 1,80,000 was disclosed separately.

11. We have heard rival contentions. On a careful consideration of the facts and circumstances of the case, and after perusal of the case laws cited before us, we hold as under.

12. The assessee admittedly is indulging in the illegal trade of a product known as N-Hexane, which is used for adulterating petrol at petrol bunkers. No books of account have been maintained. The only recourse open to the assessing officer was to estimate the undisclosed income. The assessee himself had admitted to this fact and filed block return disclosing undisclosed income from this trade. The question to be answered is whether the assessing officer was right in estimating the profit at 15% of the turnover of the assessee in this trade. To our mind, the assessing officer was fair and considerate in estimating the profit at 15% of the turnover. In fact, the assessee has benefited due to calculation mistake that has been done by the assessing officer.

The assessing officer's estimation of sales was at cost plus 596 whereas his intention was that the assessee had earned a gross profit of 15% on such sales. In that case, the total turnover of the assessee should have been estimated at cost plus 1596 or more. Nevertheless, the intention of the assessing officer is that the profit from this illegal activity would have been 15%. The logic accepted by the first appellate authority is strange. As pointed out by the learned departmental representative, no person would take such great risk of illegal trade which would make him liable for imprisonment, for earning a percentage of profit much lower than if he had done the business in an open and legal manner. As the assessing officer was not only considerate but also conservative in estimating the profit only at 15% of an underestimated figure of turnover, the assessee should not have had any grievance on the same.

13. Coming to the reliance placed on the case of Shri P. Koteswara Rao, we hold that fundamentally a profit rate adopted in the case of Shri Koteswara Rao cannot be a bench-mark, particularly in this illegal trade. Whatever might be the reason for accepting the percentage of profit in the case of Shri Koteswara Rao, to our mind, his case does not come to the rescue of the assessee. Though the same assessing officer has passed the orders in both the cases, the basis for accepting gross profit of 8.2596 in the case of Shri Koteswara Rao has not been explained or substantiated in that assessment order. Thus, we do not consider it fit, on the facts and circumstances of the case, to treat the assessment order in the case of Shri P. Koteswara Rao as a bench-mark or a comparable instance. It might have been a case of under-estimation of income of Shri Koteswara Rao, with which we are not concerned. Suffice it to say, the assessing officer's order estimating the income at 15% of the turnover determined by him in this line of trade has to be sustained and the order of the Commissioner (Appeals) to that extent, directing the assessing officer to adopt a rate of 8.25% on the turnover in the case of both these assesseees before us, be vacated.

14. Coming to the issue of telescoping, the assessee has not maintained any books of account. All the amounts received by the assessee have been deposited in the bank account and the assessee has not demonstrated as to how he claims telescoping in this case. No doubt, the Hon'ble Supreme Court in the case

(supra), held that intangible addition made in the book profit during the assessment year forms part of assessee's real income. Nevertheless, in that very same case, it was observed as follows :? It is a matter for consideration by the taxing authority in each case whether the unexplained cash deficits and the cash credits can be reasonably attributed to a pre-existing fund of concealed profits or they are reasonably explained by reference to concealed income earned in that very year. In each case, the true nature of the cash deficit and the cash credit must be ascertained from an overall consideration of the particular facts and circumstances of the case.

Evidence may exist to show that reliance cannot be placed completely on the availability of a previously earned undisclosed income. A number of circumstances of vital significance may point to the conclusion that the cash deficit or cash credit cannot reasonably be related to the amount covered by the intangible addition but must be regarded as pointing to the receipt of undisclosed income earned during the assessment year under consideration. It is open to the revenue to rely on all the circumstances pointing to that conclusion.

The ratio in all the judgments relied upon by the assessee is that secret profits or undisclosed income carried by the assessee can constitute a fund from which the assets were acquired, provided a reasonable nexus exists. Mere availability of such funds would not in all cases imply that the assessee had earned further secret profits during the relevant assessment year. It is a matter for consideration by the taxing authorities in each case to ascertain whether the unexplained cash deficits or cash credits can be reasonably attributed to a pre-existing fund of concealed profits during the relevant assessment year. In all these cases, the unexplained income was earned only during the previous year and was utilised for acquisition of assets in that year only, whereas in the case on hand it is spread over a number of years. In any event, the facts and circumstances do not point to a reasonable conclusion that telescoping could be allowed as claimed by the assessee. The very nature of the trade activities of the assessee and lack of evidence to support the contention of the assessee result in our dismissing this ground of the assessee. The order of the Commissioner (Appeals), therefore, is set aside and the order of the assessing officer is restored.

15. In the result, the appeals of the revenue are allowed and the appeals of the assesseees are dismissed.