Colorcraft Vs. the Ito

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Court : Income Tax Appellate Tribunal ITAT Mumbai

Decided On : May-12-2006

Reported in : (2007)105ITD599(Mum.)

Judge : K Singhal, D Srivastava

Appellant : Colorcraft

Respondent : The Ito

Judgement :

1. The assessee has preferred this appeal against the order of the Learned CIT Under Section 263 of the Income Tax Act, 1961 (Act).

2. The brief facts giving rise to this appeal are these: The assessee filed its income tax return for the year under consideration disclosing total income at Rs. 7,45,780/- after claiming deduction Under Section 80HHC of the Act for Rs. 69,98,537/-. The original assessment Under Section 143(3) of the Act was made by the Assessing Officer on 31.3.2003, determining the total income at Rs. 7,88,376/-.

Subsequently, the Learned CIT received a proposal from the Assessing Officer to the effect that the assessment was erroneous and prejudicial to the interest of Revenue in as much as deduction Under Section 80HHC was allowed in excess. Further, no enquiry was carried out with reference to the genuineness of the loans as well as the transactions falling Under Section 40A(2)(b) of the Act. Accordingly,

the Learned CIT issued notice Under Section 263 on the following grounds: 1. In the order Under Section 143(3), deduction Under Section 80HHC of I.T. Act of Rs. 70,46,582/- was allowed. It is seen that the eligible business profits include duty draw back of Rs. 20,64,833/-.

As per the Supreme Court decision in the case of Sterling Foods 237 ITR 579 (SC), the said amount was not derived from export activity and hence does not qualify for deduction Under Section 80HHC of I. T. Act. Further, the deduction Under Section 80HHC allowed on the duty draw back received as per proviso to Section 80HHC(3) was erroneously allowed.

2. Purchases of Rs. 49,05,984/- from M/s. Mineral India International were not verified in terms of Section 40A(2)(b) of the I. T. Act.

3. Loans appearing in the Balance Sheet and loans squared off during the year were not verified in terms of Section 68 of the I. T. Act.

After considering the reply of the assessee, the Learned CIT held that excessive deduction was allowed Under Section 80HHC for three reasons namely - (i) that the Assessing Officer should have excluded the entire export incentive of Rs. 18,99,015/- from the business profits instead of Rs. 18,58,350/- being 90% of the export incentives, (ii) that the central excise refund and sales tax set-off should have been included in the total turnover and (iii) that the central excise refund and sales tax set-off should have been excluded from the business profits as per Clause (baa) of Explanation to Section 80HHC. It was further held that there was lack of proper enquiry on the part of Assessing Officer for determining the genuineness of the loans as well as with reference to the transactions of purchase of Rs. 49,05,984/- from the sister concern M/s. Mineral India International vis-a-vis Section 40A(2)(b). Accordingly, it was held that order of the Assessing Officer was erroneous and prejudicial to the interest of Revenue. Consequently, the order of the assessment was set aside to the file of Assessing Officer for fresh adjudication after making necessary enquiries and after giving opportunity of hearing to the assessee. Aggrieved by the same, the assessee has preferred this appeal before the Tribunal.

3. The Learned Counsel for the Assessee has assailed the impugned order of the Learned CIT by raising various submissions. Firstly, it was submitted that there was no co-relation between the reason given by the Learned CIT in the show cause notice and the reasons given in the impugned order vis-a-vis the deduction Under Section 80HHC for holding that the order of the assessment was erroneous. He drew our attention to the show cause notice to point out that the reason given in the notice was that duty drawback could not be considered as profit derived from export activities in view of the Hon'ble Supreme Court judgment in the case of Sterling Foods Pvt. Ltd. (supra) while the reasons given in the impugned order are quite different for holding the order of assessment to be erroneous. Thus, the impugned order of the Learned CIT cannot be sustained in view of the judgment of the Hon'ble Andhra Pradesh High Court in the case of CIT v. G.K. Kabra 211 ITR 336, and the decision of the Tribunal in the case of Sanco Trans Ltd. 61 ITD 4. Proceeding further, it was submitted that all the details relating to the purchase transactions form sister concerned were supplied to the Assessing Officer. He drew our attention to the audit report to point out that all necessary details falling Under Section 40A(2)(b) were supplied as per Annexure-J to the audit report appearing at Page-26 of the Paper Book. Then he referred to the letter of assessee dated 26.12.2002 addressed to the Assessing Officer to point out that date-wise details were furnished in respect of bills issued by the sister concern M/s. Mineral India International. This letter appears at Page-42 of the Paper Book. In view of the same, it was submitted that proper enquiry was made by the Assessing Officer and, therefore, the assessment order could not be said to be erroneous.

5. Proceeding further, it was submitted that necessary details in respect of each loan falling Under Section 269SS of the Act were furnished in Annexure-0 to the audit report. Then he referred to Page-39 of the Paper Book to point out that Assessing Officer had made enquiries vide letter dated 9.11.2001 by asking the assessee to furnish the details regarding unsecured loans along with the confirmation letters and Permanent Account Numbers of the creditors. According to him, such information was supplied to the Assessing Officer. Hence, according to him, such loans were accepted by the Assessing Officer after making proper enquiries.

6. Proceeding further, he also relied on the judgment of the Hon'ble Bombay High Court in the case of CIT v. Gabriel India Ltd. 203 ITR 108, for the proposition that no adverse inference can be drawn merely because that elaborate discussion is not made in the assessment order.

He also referred to the judgment of the Hon'ble Patna High Court in the case of ACIT v. Bhari Bros P. Ltd. 154 ITR 244 and the judgment of the Hon'ble Gujarat High Court in the case of DCIT v. Rohini Builders 256 ITR 360, for the proposition that if the loan is received by cheque, then the onus upon the assessee is said to be discharged and, therefore, it could not be said, in the present case, that proper enquiry was not made. He also relied on the judgment of the Hon'ble Supreme Court in the case of Malabar Industrial Co. Ltd. v. CIT 243 ITR 83, for the proposition that even if two views are possible and the assessment order is in consonance with one of the views, then the order of assessment cannot be said to be erroneous.

7. On the other hand, the Learned D.R has vehemently relied on the reasoning given by the Learned CIT. Further, he relied on the judgment of the Hon'ble Supreme Court in the case of Smt. Taradevi Agrawal 88 ITR 323 and the judgment of the Hon'ble Delhi High Court in the case of Gee Vee Enterprises 99 ITR 375, for the proposition that lack of proper enquiry on the part of Assessing Officer would result assessment order to be erroneous and prejudicial to the interest of the Revenue.

Proceeding further, it was submitted by him that mere collection of information is not sufficient. It is the duty of the Assessing Officer to apply his mind to the evidences so collected and ascertain whether such material is sufficient and in consonance with the provisions of the Act. He then drew our attention to the details filed by the assessee and reference to its claim Under Section 40A(2)(b). According to him, the details of bills issued by the sister concerns were not sufficient evidence for coming to the conclusion that expenditure incurred by the assessee is reasonable to the market price. Since the Assessing Officer did not make further enquiries with reference to the reasonableness of the price paid by the assessee against the purchases made from the sister concerns, there was

failure on the part of the Assessing Officer to make proper enquiries. Similarly, it was further submitted that mere confirmations and payment by cheque is not sufficient to prove the creditworthiness of the creditors and the genuineness of the loan transactions. According to him, it is the settled legal position that assessee is required to prove identity and capacity of the cash creditors as well as the genuineness of the transactions. It was pointed out by him that there was no evidence on record to prove the genuineness of the transactions as well as the creditworthiness of the cash creditors. Thus, there was lack of proper enquiry on the part of Assessing Officer. In view of the above arguments, it was submitted by him that order of the Learned CIT be upheld.8. Rival submissions of the parties have been considered carefully in the light of the material placed before us and the case law referred to. The first question for our consideration is whether the order of the Learned CIT Under Section 263 can be upheld where reasons given in the order for holding the assessment order as erroneous and prejudicial to the interest of Revenue are different from the reasons given in the show cause notice issued to the assessee. In our opinion, the answer is in the negative for the reasons given hereafter. The provisions of Section 263 itself provide that an opportunity is to be provided to the assessee before passing an order. That means, that assessee is required to reply to the reasons given by the Learned CIT in show cause notice.

Consequently, the order of the Learned CIT must be confined to reasons given in the show cause notice and, therefore, order of the Assessing Officer cannot be held to be erroneous on different ground. If the Learned CIT intends to deviate from the reasons mentioned in the show cause notice, then before taking any decision, he must confront to assessee fresh reasons which he may in his mind and then allow assessee a fresh opportunity. The opportunity to be granted must be effective and cannot be an empty formality. A person, who is required to show cause, must know the basis on which action is proposed. Obviously, therefore, the notice issued must indicate the reasons on which the order of assessment is considered to be erroneous and prejudicial to the interest of Revenue Rawani Dal & Flour Mills v. CST 86 STC 409 (Ori.). This means, there must be nexus between the reasons given in the show cause notice and the order of the Learned CIT Under Section 263. Consequently, in our opinion, it has to be held that order of the Learned CIT would be bad-in-law where such order is not passed on the reasons

given in the show cause notice.

9. The view taken by us is fortified by the judgment of the Hon'ble Andhra Pradesh High Court in the case of CIT v. G.K. Kabra 211 ITR 336.

In that case, the notice Under Section 263 related to the assessment of capital gain while the final order related to the inference of escapement of hire charges. The Tribunal held that the order of Learned CIT Under Section 263 was vitiated in law and, therefore, had to be cancelled. The Hon'ble High Court upheld the order of the Tribunal after making the following observations.

Inasmuchas as the Commissioner had not chosen to show these two points as the errors in making the final order and the final order under Section 263 refers only to the inference of hire charges being exigible to tax which was not mentioned at all in the show cause notice, obviously the assessee had no opportunity to meet that point. Moreover, a reading of the show cause notice cannot give the assessee or even us, for that matte, any indication with reference to the hire charges which are sought to be assessed by the revision.

Similar view has been taken by the Tribunal, Madras Bench in the case of Sanco Trans Ltd. 61 ITD 317. The relevant portion of the same is reproduced as under: The Hon'ble Calcutta High Court in the case of CIT v. General Trade Agencies [1973] Tax LR 1383 held that where the show cause notice did not fairly indicate the grounds used by the Commissioner in his order under Section 263, the assessee was deprived of fair opportunity to show cause against proposed action and in such a case, the revisional order of the Commissioner cannot be sustained.

The same Calcutta High Court in the case of Bagsu Devi Bafna v. CIT [1966] 62 ITR 506, affirmed in Bagsu Devi Bafna v. CIT , held that the Commissioner must disclose in his notice to the assessee, the grounds on which he proposes to revise, to enable the assessee to show cause and to give him an opportunity of being heard. The Hon'ble Orissa High Court held in the case of Rawani Dal & Flour Mills v. CST [1992] 86 5TC 409 that the opportunity to be granted must be effective, that it cannot be an empty formality, that a person who is required to show cause must know the basis on which the action is proposed and that

obviously, therefore, the notice issued must indicate as to on what grounds the order is considered erroneous insofar as it is prejudicial to the interests of the Revenue. Since the under Section 263 dated 22.3.1990 did not indicate the ground used by the Commissioner, in his order under Section 263 dated 30.3.1990, the impugned order Under Section 263 cannot be sustained.

The Hon'ble Gujarat High Court, though rendered in penalty proceedings in the case of CIT v. Lakhdhir Lalji 85 ITR 77, cancelled the penalty by giving similar reasonings. The relevant portion of the judgment is quoted below: Held, that the penalty proceedings had been commenced against the assessee on a particular footing, viz. concealment of particulars of income but the final conclusion for levying the penalty was based on a different footing altogether viz. on the footing of furnishing inaccurate particulars of income. Under the circumstances, it could not be said that the assessee had been given reasonable opportunity of being heard before the order imposing the penalty was passed. The very basis for the penalty proceedings against the assessee initiated by the Income Tax Officer disappeared when the Appellate Assistant Commissioner held that there was no supervision of income by the assessee. The conclusion of the Tribunal that the Inspecting Assistant Commissioner had no jurisdiction to impose a penalty under Section 271(1)(c) for concealment of income was correct. [As per Head Note In the present case, the reason given in the show cause notice was that duty drawback received by the assessee could not be considered as profit derived from export in view of the Supreme Court judgment in the case of Sterling Foods Pvt. Ltd. 247 ITR 579 and, therefore, the said amount did not qualify for deduction Under Section 80HHC. However, the order Under Section 263 held the assessment order as erroneous on different grounds namely - (i) the Assessing Officer should have excluded the export incentives of Rs. 18,99,015/- instead of Rs. 18,58,350/-, (ii) Central Excise refund and Sales Tax set-off should have been excluded from the business profits under Clause (baa) of Explanation to Section 80HHC and (iii) Central Excise refund and Sales Tax set-off should have been included in the total turnover. However, there is no mention of the basis mentioned in the show cause notice.

This clearly shows that there was no nexus between the reasons given in the show cause and the reasons given in the impugned order for holding the order of Assessing Officer as erroneous qua deduction Under Section 80HHC. Therefore, following the reasons given by us in the preceding paras, we quash the order of the Learned CIT (A) to the extent mentioned above.

10. The next question for our consideration is whether there was lack of enquiry and non-application of mind on the part of Assessing Officer vis-a-vis the issue relating to unsecured loans and excessive allowance of expenditure vis-a-vis Section 40A(2). There is no dispute that lack of enquiry would render the order of assessment as erroneous and prejudicial to the interest of Revenue as held by the Hon'ble Supreme Court in the case of Rampyaridevi Sarogi 67 ITR 84 and in the case of Taradevi Agrawal 88 ITR 323. The lack of enquiry would include not only the situation where no enquiry is made but would also include the situation where no proper enquiry is made considering the facts of the case. Whenever expenditure is claimed by the assessee as deduction, the onus is on the assessee to prove its genuineness. However, where payment is made to the persons mentioned in Section 40A(2), then it is the duty of the Assessing Officer to make proper enquiry to ascertain whether such expenditure is reasonable with reference to the prevailing market price. Similarly, where any receipt is claimed to be exempt from taxation, it is the duty of Assessing Officer to ascertain whether conditions for allowing expenditures are fulfilled or not. The duty of the Assessing Officer is to collect the correct tax due from the assessee -neither a penny more nor a penny less. Therefore, if he fails in performing in his duty, then his order can be considered as erroneous and prejudicial to the interest of Revenue. In our opinion, mere collection of material is not enough in discharging of such duty.

It is also the duty of the Assessing Officer to evaluate the material or evidence collected and then ascertain whether such materials are enough to sustain the claim of the assessee.

11. In the above backdrop, let us examine the facts of the present case. Regarding the payments made by the assessee falling Under Section 40A(2)(b), the assessee had given details of sister concerns to whom the payments were made

(Page-26 of the Paper Book). He also gave details of bills issued by M/s. Mineral India International (Pages-42 and 43 of Paper Book). This detail provides the dates and invoice numbers as well as the total amount of purchases. No other information was given by the assessee. In our opinion, this information by itself is not sufficient for holding that payments made to sister concern Under Section 40A(2)(b) was reasonable and not excessive. Whether the payment was excessive or not would depend upon the prevalent market prices. However, the Assessing Officer did not make any enquiry regarding prevalent market price of the goods purchased by the assessee from the sister concern. In the absence of such enquiry on the part of Assessing Officer, in our opinion, the assessment order became erroneous. Therefore, the order of the Learned CIT (A) has to be held to be valid in this regard.

12. Regarding the issue of unsecured loans, the audit report, vide Annexure-O, provides the details of loans, accepted by the assessee, exceeding the limit prescribed in Section 269SS of the Act (Pages-30 and 31 of the Paper Book). It also appears that the Assessing Officer asked the assessee to furnish the details of unsecured loans along with confirmation letters and the Permanent Account Numbers of the cash creditors (Page-39 of the Paper Book). In response to the same, the assessee had furnished the copies of the accounts of these cash creditors in the books of assessee on which such cash creditors had confirmed such accounts. Their addresses and Permanent Account Numbers are given on such certificates. It also appears that the transactions were by cheques. So, the question is whether there was any lack of enquiry on the part of the Assessing Officer. It is the settled legal position that in the case of cash credits appearing in the books of assessee, the onus is on the assessee to prove the identity and creditworthiness of the cash creditors as well as the genuineness of the transactions. The evidence produced before the Assessing Officer nowhere provides the creditworthiness of the cash creditors. No doubt, the payments were by cheques but that by itself does not prove the creditworthiness of the assessee. Neither the Bank statement of cash creditors nor their Balance Sheet were examined. Even the Assessing Officer had not made any enquiry from the concerned Assessing Officers with whom they were assessed. Therefore, in our opinion, the Assessing Officer failed to make proper enquiries before accepting the

explanation of the assessee. Thus, there was lack of proper enquiry on the part of the Assessing Officer.

13. The Learned Counsel for the Assessee has relied on the two decisions of High Courts namely - (i) 154 ITR 244 (Pat.) and (ii) 256 ITR 360 (Guj.). These cases are not on the point before us. The question before the Patna High Court was whether addition could be made where the assessee had disclosed the names of the creditors and the names of the Banks on which the cheques were drawn. The Court held that the assessee had discharged the primary onus and the onus shifted to the Department to verify the same. This itself shows that the Assessing Officer was required to make enquiry before rejecting the case of assessee. Similarly, in the case before the Gujarat High Court. Their Lordships referred to Supreme Court judgment in the case of Orissa Corporation 159 ITR 78 and observed that where names and addresses of the creditors and GIR numbers are disclosed, then the burden shifted to the Department to establish the Revenue's case and in order to sustain the addition, the Revenue has to pursue the enquiry and to establish the lack of creditworthiness (Pages 369 of 256 ITR). This judgment of the Supreme Court also shows that the Department is required to make enquiries to prove the lack of creditworthiness before making any addition Under Section 68. Therefore, these two decisions relied upon by the assessee's counsel do not help the case of the assessee. In our opinion, the fact of creditworthiness must be established and the primary onus is on the assessee to establish the same. In the present case, no evidence was furnished regarding the creditworthiness of the parties. Even otherwise, in such situation, the Assessing Officer should have made enquiries in this regard before accepting the explanation of the assessee. Therefore, in our opinion, there was lack of enquiry on the part of Assessing Officer and the same rendered the assessment order to be erroneous and prejudicial to the interest of Revenue. The order of the Learned CIT (A) is, therefore, sustained on this issue.

14. In view of the above discussion, the order of the Learned CIT Under Section 263 is partly quashed. Consequently, the appeal of the assessee is partly allowed.