(2013) 10 AHC CK 0124

Allahabad High Court (Lucknow Bench)

Case No: Income Tax Appeals Nos. 130, 135 of 2006, 93, 94, 107, 108, 127 to 129, 130, 131 of 2007 and 44 of 2009

Commissioner of Income Tax	APPELLANT
Vs	
Sahu Construction P. Ltd.	RESPONDENT

Date of Decision: Oct. 8, 2013

Citation: (2014) 362 ITR 609

Hon'ble Judges: Satish Chandra, J; Rajiv Sharma, J

Bench: Division Bench

Final Decision: Disposed Of

Judgement

Dr. Satish Chandra, J.

All the present appeals have been filed by the Department u/s 260A of the income tax Act, 1961, against the different judgments and orders passed by the income tax Appellate Tribunal, Lucknow. The details of the income tax appeals are as under:

On May 27, 2009, a co-ordinate Bench of this court has admitted income tax Appeal No. 44 of 2009, on the following substantial questions of law:

I. Whether, on the facts and in the circumstances of the case, the learned income tax Appellate Tribunal has erred in law in canceling the penalty of Rs. 50,00,000 levied u/s 271(1)(c) of the income tax Act without appreciating that willful concealment is not an essential ingredient for attracting penalty as has been held by the Hon''ble Supreme Court of India in the case of Union of India (UOI) and Others Vs. Dharamendra Textile Processors and Others, ?

II. Whether, on the facts and in the circumstances of the case, the learned income tax Appellate Tribunal has erred in law in canceling the penalty of Rs. 50,00,000 levied u/s 271(1)(c) of the income tax Act without appreciating that false or exaggerated claim of expenditure or deduction is very well covered under the concealment of income/furnishing of inaccurate particulars of income thereby making the assessee liable for penalty?

III. Whether, on the facts and in the circumstances of the case, the learned income tax Appellate Tribunal has erred in law in canceling the penalty of Rs. 50,00,000 levied u/s 271(1)(c) of the income tax Act without appreciating that in quantum appeal the rejection of books of account by the Assessing Officer has been upheld by the learned income tax Appellate Tribunal itself. The learned income tax Appellate Tribunal has further failed to appreciate that specific defects in the books of account of the assessee have been detected by the Assessing Officer which is a clear proof of concealment of income/furnishing of inaccurate particulars of income?

2. In income tax Appeals Nos. 130 of 2006, 94 of 2007, 107 of 2007, 108 of 2007 and 93 of 2007, different co-ordinate Benches have admitted the respective appeals on the following substantial questions of law:

I. Whether, on the facts and in the circumstances of the case, the learned income tax Appellate Tribunal was justified in law in deleting the penalty imposed u/s 271(1)(c) of the income tax Act, 1961, when in quantum appeal the rejection of books of account by the Assessing Officer for the reason of particulars of income being inaccurate had been upheld and application of net profit rate to the extent of 3.5 per cent had also been confirmed by them?

II. Whether, on the facts and in the circumstances of the case, the learned income tax Appellate Tribunal was justified in deleting the penalty u/s 271(1)(c) when both the pre-conditions despite being mutually exclusive, for imposition of such penalty, were fully satisfied in the case?

3. On November 14, 2007, a co-ordinate Bench of this court has admitted income tax Appeals Nos. 127 of 2007, 128 of 2007, 129 of 2007, 130 of 2007 and 131 of 2007, on the following substantial questions of law:

I. Whether, on the facts and in the circumstances of the case, the income tax Appellate Tribunal was justified in law and on facts in reducing the estimated net profit to 3.5 per cent as against the 10 per cent rate applied by the Assessing Officer and further allowing depreciation from it?

II. Whether, on the facts and in the circumstances of the case, the income tax Appellate Tribunal was right in law in estimating the rate of net profit at a substantially reduced rate resulting in a situation where the relief is more than the addition made and has also resulted into estimated loss?

III. Whether, on the facts and in the circumstances of the case, the income tax Appellate Tribunal was right in law in not appreciating that it is a well settled principle that where the estimate by the Assessing Officer is based on a rational basis, prima facie the Assessing Officer is the best judge of the situation and the Commissioner of income tax (Appeals) could not substitute her judgment for that of the Assessing Officer unless there were compelling reasons for doing so (The

Commissioner of Sales Tax, Madhya Pradesh Vs. H.M. Esufali, H.M. Abdulali, Siyaganj, Main Road, Indore,)?

IV. Whether, on the facts and in the circumstances of the case, the income tax Appellate Tribunal was justified in law in stretching the definition of net profit so as to conclude that depreciation and interest are liable to be deducted subsequent to it, contrary to the basic principles of accounting especially when the net profit has been estimated after considering all the expenses and depreciation, etc., by the Assessing Officer?

4. The facts and circumstances in all the appeals are identical. Hence, all the appeals are disposed of by this consolidated order for the sake of brevity. However, the dates, figures, etc., have been taken from the leading I.T.A. No. 44 of 2009 for the purpose of adjudication of the present appeals.

5. The brief facts of the case are that during the assessment years under consideration, the assessee has worked out the profit as per the provision u/s 115JA of the income tax Act. The assessee has not furnished the details as asked by the Assessing Officer so the books of account were rejected by the Assessing Officer. When the books of account were rejected, the Assessing Officer has estimated the net profit rate at the rate of 10 per cent of the gross receipts and made the additions accordingly. In appeal, the Commissioner of income tax (Appeals) reduced the net profit rate to 8 per cent on estimate basis, but did not allow depreciation as claimed. Thus, the Commissioner of income tax (Appeals) has given partial relief to the assessee. However, in second appeal, the income tax Appellate Tribunal has further reduced the net profit rate at 3.5 per cent and also allowed the depreciation as claimed from the contract receipts.

6. When the Assessing Officer has made addition on estimate basis for the same assessment years, then he has also levied the penalty u/s 271(1)(c) of the income tax Act. income tax Appeals Nos. 127 of 2007, 128 of 2007, 129 of 2007, 130 of 2007, 131 of 2007 and 135 of 2006 are pertaining to the quantum, i.e., additions which were made on estimate basis. The remaining income tax Appeals Nos. 94 of 2007, 130 of 2006, 93 of 2007, 107 of 2007, 108 of 2007 and 44 of 2009 are related to penalty u/s 271(1)(c) which were rejected by the Tribunal. Being aggrieved, the Department has filed the present appeals.

7. With this background, Sri D.D. Chopra, learned counsel for the Department, on the strength of written submissions, submits that the Tribunal has reduced the net profit rate by following its earlier order. He further submits that each assessment year will have to be dealt separately. He also submits that the Tribunal has passed the order in an arbitrary manner without considering the finding of the Assessing Officer.

8. Further, he submits that Hon''ble Supreme Court in the case of The Commissioner of Sales Tax, Madhya Pradesh Vs. H.M. Esufali, H.M. Abdulali, Siyaganj, Main Road,

Indore, , observed that in estimating any escaped turnover, it is inevitable that there is some guess work. He further submits that the Tribunal has not recorded the reasons which are required as per the ratio laid down in the case of Commissioner of Income Tax Vs. Palwal Co-operative Sugar Mills Ltd., , which reads as under (headnote):

Every judicial/quasi-judicial body/authority must pass a reasoned order which should reflect the application of mind of the concerned authority to the issues/points raised before it. The requirement of recording reasons is an important safeguard to ensure observance of the rule of law. It introduces clarity, checks the introduction of extraneous or irrelevant considerations and minimises arbitrariness in the decision making process. Another reason which makes it imperative for quasi-judicial authorities to give reasons is that their orders are not only subject to the right of the aggrieved persons to challenge them by filing statutory appeal and revision but also by filing writ petition under article 226 of the Constitution. Such decisions can also be challenged by way of appeal under article 136 of the Constitution of India. The High Courts have the power to issue writ of certiorari to quash the orders passed by quasi-judicial authorities/tribunals. Likewise, in appeal the Supreme Court can nullify such order/decision. This power of judicial review can be effectively exercised by the superior courts only if the order under challenge contains reasons. If such order is cryptic and devoid of reasons, the courts cannot effectively exercise the power of judicial review.

9. It is also the submission of the learned counsel that it is the duty of the Tribunal to deal with and dispose of the issues of the facts in detail and then give categorical findings for its eventual conclusions as per the ratio laid down in the case of Commissioner of Income Tax Vs. Mandsour Ferro Alloys Ltd., , which reads as under (headnote):

The Tribunal being the last court of facts in the hierarchical system, it is its legal duty rather legal obligation to deal with and discuss the issues of fact in detail and then give categorical findings for its eventual conclusion. A casual approach while deciding the issue exhibits non-application of mind. It is much more so when the factual finding recorded by the Commissioner (Appeals) is assailed specifically by the assessee in the appeal on the facts. It must appear from the order that sincere efforts were made to go into the factual arena and then keeping in view the legal position applicable to the facts of the case, a categorical finding is recorded by the Tribunal.

10. On the other hand, the learned counsel for the assessee, Sri Aruneshwar Gupta, assisted by Sri Sushil Kumar and Sri Sural Kumar, has justified the impugned orders. He submits that the Assessing Officer has rejected the books of account and has applied the net profit at 10 per cent of the gross receipts. Finally, the Tribunal has reduced the net profit rate at 3.5 per cent plus depreciation. All the appeals were decided after insertion of section 44AD of the income tax Act. However, this Hon''ble

High Court in I.T.A. Nos. 134 of 2006 and 129 of 2006, in the assessee''s case observed that section 44AD is not applicable as the turnover is less then 40 lakhs. So, no substantial questions of law were involved. This order has attained the finality. Lastly, he made a request for dismissal of the appeals.

11. We have heard the parties at length and gone through the material available on record. It is an undisputed fact that the Assessing Officer has rejected the books of account and estimated the net profit rate at the rate of 10 per cent of the gross contract receipts. During the assessment years under consideration, the Commissioner of income tax (Appeals) has reduced the same and, finally, the Tribunal has estimated the net profit at 3.5 per cent of gross receipts. In addition, the Tribunal has also allowed the depreciation on the contract receipts.

12. It is also a submission of the learned counsel that as per Central Board of Direct Taxes Circular No. 29-D (XIC-14) [F. No. 45-239-65-ITJ] dated August 31, 1965, if the profits are estimated, and prescribed particulars have been furnished by the assessee, the depreciation allowance should be separately worked out and the deductions should be separately deducted from the profit, but the fact remains that in the instant cases, if the net profit at 3.5 per cent is taken and depreciation separately allowed then the income of the assessee will come to negative, as appears from the details (examples) mentioned below for the assessment years 1994-95 and 1996-97:

13. From the above, it appears that the net effect of the decision of the income tax Appellate Tribunal is that it has resulted into a negative figure or marginal profit in other assessment years. Thus, the relief appears more than the rate of net profit at 10 per cent estimated by the Assessing Officer. In such cases, the intention and purpose behind the relevant provisions in the statute, i.e., to estimate the income and not to estimate negative income (loss) is defeated. In the instant cases, the impugned orders of income tax Appellate Tribunal have resulted into just opposite to this.

14. Secondly, the income tax Appellate Tribunal has further erred in allowing depreciation over and above the net profit of 3.5 per cent decided by them. As per the definition of net profit given in the Law Lexicon by P. Ramanatha Aiyer page 1300 means the surplus left after deducting for all losses. Further, "Net profits of a company is the sum divisible after the discharging or making provision for every outgoing expense properly chargeable against the period, whether a year or less, for which the profits are to be calculated" (per Kekewich J. Glassiet v. Rolls 42 Ch. D 453)

15. Thus, the term "net profit" by its very name is an all inclusive one or in a nut-shell it is the profit which has been arrived at after netting off of income over the expenditure, meaning thereby that whatever expenses or notional expenses were due and to be deducted from the income of the firm or the company had been done

prior to deriving the final figure, i.e., profit. It is the same profit that is offered for taxation. Therefore, when the Assessing Officer applied the rate of 10 per cent for estimating the net profit then the depreciation is deemed to have already been given especially when the Assessing Officer in his concluding line of the assessment order had clearly mentioned that "Since no deduction from section 30 to section 38 including depreciation is allowable as per section 44AD, in the case of small contractors, therefore no deduction on account of depreciation, etc., will be allowed, on net profit, in this case also". Thus, the estimated net profit includes depreciation and it cannot be claimed separately.

16. Further, the case law on which the income tax Appellate Tribunal has placed its reliance is also distinguishable on two grounds:

17. Firstly, Circular No. 29D, dated August 31, 1965, which prescribed to allow depreciation out of the estimated profit, is not applicable, as rule 5AA of the income tax Rules has been omitted with effect from April 2, 1987. This aspect was discussed by this High Court and it was observed in the case of Commissioner of Income Tax Vs. Bishambhar Dayal and Co., : "the income tax Appellate Tribunal relied upon a circular of the Central Board of Direct Taxes No. 29D(xix) of 1965, F. No. 45/239/65-ITC, dated March 31, 1965. Under this circular, the Board had issued instructions that where income is proposed to be computed by applying a net rate and the assessee has furnished the prescribed particulars for the claim in respect of depreciation, the depreciation should be allowed separately and deducted out of the gross profits. The order of the income tax Appellate Tribunal is in conformity with the circular issued by the Central Board of Direct Taxes. No provision of the income tax Act was brought to our notice which makes the claim to depreciation inadmissible where the income is computed by applying the flat rate".

18. Secondly, subsequent to the assessment year 1994-95, in such matters the basic principle as enumerated in section 44AD of the income tax Act, 1961, is taken to be applicable wherein the matrix of estimation of profit on gross receipts have been laid down for the civil construction work. Subsection (2) of section 44AD reads under:

Any deduction allowable under the provisions of sections 30 to 38 shall, for the purposes of subsection (1), be deemed to have been already given full effect to and no further deduction under those sections shall be allowed:

Provided that where the assessee is a firm, the salary and interest paid to is partners shall be deducted from the income computed under subsection (1) subject to the conditions and limits specified in clause (b) of section 40.

and subsection (3) reads that:

The written down value of any asset used for the purpose of the business referred to in subsection (1) shall be deemed to have been calculated as if the assessee had

claimed and had been actually allowed the deduction in respect of the depreciation for each of the relevant assessment years.

19. The Hon''ble High Court in the case of Commissioner of Income Tax Vs. Chopra Brothers India (P.) Ltd., observed that after allowing 8 per cent profit u/s 44AD, no further deduction is allowable as per section 44AD(2).

20. In the case of Commissioner of Income Tax Vs. Gian Chand Labour Contractors, , it was observed that no further separate deduction is allowable as per sections 29, 144 and 145 of the Act. The relevant portion of the judgment reads as under (headnote):

Section 145 of the income tax Act, 1961, provides for computation of income u/s 29 on the basis of books of account and methods of accounting regularly followed by the assessee. However, where the Assessing Officer is not satisfied with the correctness or completeness of the books, he may reject them and estimate the income to the best of his judgment in accordance with the provisions of section 144 of the Act. When an estimate is made to the best judgment of an Assessing Officer, he substitutes the income that is to be computed u/s 29 of the Act. Once best judgment assessment is made by fixing a rate of net profit, the assessee''s claim for deduction on account of expenses cannot be deemed to have been ignored. The net profit rate is applied after taking into consideration all factors and it accounts for all the deductions which are referred to u/s 29 and are deemed to have been taken consideration while making such estimate.

21. In the case of Indwell Constructions Vs. Commissioner of Income Tax, , the hon''ble High Court observed as under (headnote):

The pattern of assessment under the income tax Act, 1961, is given by section 29 which states that the income from profits and gains of business shall be computed in accordance with the provisions contained in sections 30 to 43D of the Act. Section 40 provides for certain disallowances in certain cases notwithstanding that those amounts are allowed generally under other sections. The computation u/s 29 is to be made u/s 145 on the basis of the books regularly maintained by the assessee. If those books are not correct or complete, the income tax Officer may reject those books and estimate the income to the best of his judgment. When such an estimate is made, it is in substitution of the income that is to be computed u/s 29. In other words, all the deductions which are referred to u/s 29 are deemed to have been taken into account while making such an estimate. This will also mean that the embargo placed in section 40 is also taken into account.

Where the books of account have been rejected, the Revenue cannot rely on the same books for addition of an exact item (of expenditure) in the profit and loss account.

22. However, regarding the validity of net profit rate on estimated basis, it appears that in the instant case, the Assessing Officer has made the additions on the estimate basis and the Commissioner of income tax (Appeals) has reduced the same on estimate basis and the Tribunal has further reduced on estimate basis.

23. Needless to mention that the estimate is question of fact as per the ratio laid down in the cases of Commissioner of Customs (Import) Vs. Stoneman Marble Industries and Others, ; Vijay Kumar Talwar Vs. Commissioner of Income Tax, Delhi, ; New Plaza Restaurant Vs. Income Tax Officer, and Sanjay Oilcake Industries Vs. Commissioner of Income Tax, .

24. In the light of above discussion and by considering the facts and circumstances of the case, we uphold the net profit at 3.5 per cent estimated by the Tribunal, being question of fact. But we direct the Assessing Officer that no separate deduction like depreciation will be allowed. Thus, when the net profit is made on estimate basis after rejecting the books of account, then no deduction including depreciation is allowed.

25. In the instant cases, when the books of account were rejected, then the assessee is not entitled for the depreciation separately on the same set of books of account which have no value after its rejection. Hence, we modify the impugned order passed by the Tribunal pertaining to the addition and direct that the depreciation will not be allowed when the books of account were rejected and net profit rate was estimated.

26. When we uphold the estimation made by the Tribunal, then penalty orders, which are consequential to the quantum appeals, have become meaningless. Therefore, the penalty orders are not sustainable. So, the Tribunal order in this regard is hereby upheld.

27. The answer to the substantial questions of law is partly in favour of the assessee as well as the Department. In the result, income tax Appeals Nos. 94 of 2007, 130 of 2006, 93 of 2007, 107 of 2007, 108 of 2007 and 44 of 2009 are hereby dismissed and income tax Appeals Nos. 127 of 2007, 128 of 2007, 129 of 2007, 130 of 2007, 131 of 2007 and 135 of 2006 pertaining to quantum are hereby partly allowed.