

Sheraton Apparels, Max Corporation and Tressa Fashion Vs Assistant Commissioner of Income Tax

Court: Bombay High Court

Date of Decision: May 3, 2002

Acts Referred: Evidence Act, 1872 " Section 34

Finance Act, 2001 " Section 2(12A)

Income Tax Act, 1961 " Section 271(1)

Citation: (2002) 5 BomCR 19 : (2003) 1 BOMLR 888 : (2002) 175 CTR 651 : (2002) 256 ITR 20 : (2003) 1 MhLj 302 : (2002) 123 TAXMAN 238

Hon'ble Judges: V.C. Daga, J; J.P. Devadhar, J

Bench: Division Bench

Advocate: V.H. Patil, Jyoti Dialoni and V.S. Joshi, for the Appellant; R.V. Desai, P.S. Jetly and B.M. Chatterjee, instructed by H.D. Rathod, for the Respondent

Final Decision: Dismissed

Judgement

V.C. Daga J.

1. These three appeals have been filed against the common order dated February 22, 2000, passed by the Income Tax Appellate Tribunal, C-

Bench, Mumbai ("the Tribunal" for short). The Tribunal, while confirming the said order, also upheld levy of penalty u/s 271(1)(c) of the Income

Tax Act, 1961 ("the Act" for short).

Factual matrix

2. The factual matrix lies in a narrow compass and it is this :

3. The appellants are partnership firms engaged in the business of manufacturing garments and operate as semi wholesalers. The appellant is a part

of a group concern belonging to one Shah family. Returns for the assessment years 1986-87 and 1988-89 were filed by the assessee. In

pursuance thereof assessments were finalised.

4. There was a search and seizure operation u/s 132 of the Act, carried out in the shop premises of all the appellants after the returns were filed by

them. One of such seizure operations was carried out at the residence of partners of the group concern, viz., Shri Madhukar R. Shah, Shri Ramesh

R. Shah and Shri Kantilal R. Shah. Simultaneously, there was a survey action u/s 133A of the Act at the factory premises of these group concerns :

In the course of search and seizure operations, certain documents, papers and records including certain diaries were seized.

5. Subsequently, the seized material was scrutinised and as a result of the scrutiny, the following unaccounted income has been worked out:

Rs. Rs.

i) Pack of loans worked out on the basis of seized material... 40,89,484

{ii) Unexplained jewellery... 2,91.524

1. Oral judgment

(iii) Unexplained cash... 39,127

(iv) On money paid in respect of the following properties :

(a) Office Nos. 14, 15, 16, Malad Shopping Centre, 2,51,000

Malad, Bombay

(b) Office No. 607, Paramsrampur Chambers, Anand 1,15,000

Road, Malad, Bombay -----

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3,66.000

Estimated at 80 per cent. 236,000

46,56,135

6. The assessee group admitted the above unaccounted income and offered to disclose the additional income in the hands of various firms in

various years, broadly on the basis of entries recorded in diaries, when their statements were recorded u/s 132(4) of the Act. The total disclosure

made at the time of search was to the tune of Rs. 47,62,860. The papers and documents found during the search were attached. The same were

scrutinised by the Income Tax Department. Based on such scrutiny, the Department arrived at Rs. 46,56,135 as undisclosed income of the said

firm.

7. On the basis of the disclosures, all the group concerns including the appellants herein chose to file revised returns on February 19, 1991. These

returns and additional income disclosed therein were accepted by the Assessing Officer while passing the assessment orders u/s 143(3) of the Act

during the assessment proceedings of the respective concerns for the respective years. In the assessment orders, the Assessing Officer ordered

initiation of penalty proceedings u/s 271(1)(c) of the Act.

8. On the day of the assessment orders, the notices u/s 274 read with Section 271 proposing levy of penalty u/s 271(1)(c) of the Act were issued

as the Assessing Officer was of the opinion that penalty u/s 271(1)(c) of the Act has to be levied ; since the returns for the other years including the

assessment years in question, were filed beyond the time limit prescribed for filing the return u/s 139(1) of the Act, and that the appellants were not

entitled to claim benefit of Explanation 5 to Section 271(1)(c) of the Act.

9. Aggrieved by the aforesaid orders, the appellants preferred an appeal before the first appellate authority, i.e., the Commissioner of Income Tax

(Appeals), who confirmed the levy of penalty vide order dated June 26, 1995, for the respective assessment years.

10. The aforesaid orders were unsuccessfully challenged before the Tribunal. The appeals preferred by all the appellants were disposed of by the

common order since identical facts and issues were involved. That is how the present appeals were filed. So this single judgment will dispose of all

the three appeals under consideration.

11. Learned counsel Shri Patil, appearing for the appellants, in all the appeals raised a solitary contention that the diaries on the basis of which the

income was estimated and offered ought to have been regarded as books of account for the purposes of Clause (1) of Explanation 5 to Section

271(1)(c) of the Act. In his submission, the appellants were clearly entitled to the benefit of the exception provided in Clause (1) of Explanation 5

to Section 271(1)(c), since the transactions resulting in such additional income were found to have been recorded in the books of account, as such

no penalty was leviable,

Substantial question of law :

12. The substantial question of law sought to be raised in the memo of appeal reads as under :

Whether, on the facts and in circumstances of the case and law, the diaries, on the basis of which the additions were made could be regarded as

books of account for the purposes of Clause (1) of Explanation 5 to Section 271(1)(c) of the Act, so as to provide immunity to the appellants ?

Arguments :

13. Learned counsel for the appellants/assessee submitted that the subject-matter of levy of penalty under Explanation 5 is the income which

represents the money, bullion, jewellery or other valuable articles or things found at the time of search. He further submitted that so far the income

which represents money, having been recorded in the diaries seized during the course of search no penalty could be levied under Explanation 5. In

other words, the defence of the appellant is that during search and seizure certain diaries having been seized, wherein all the transactions of the

appellants were recorded, such diaries ought to have been treated as books of account, and the appellants/ assessees ought to have been given

benefit of the exception carved out in Sub-clause (1) Explanation 5 to Section 271(1)(c), holding that no penalty was leviable. Learned counsel for

the appellants stated that a disclosure of income was made, out of which 85 per cent, was in respect of inflation of expenditure and 15 per cent,

represented suppressed sales, which were not taken to the fair cash book. In the submission of the appellants, books of account generally mean

those books which contain the relevant transaction of business or profession on the basis of which the profits for a given period are computed.

According to the appellants, books of account would normally include cash books, bank books, ledgers, day books, journal books, etc. Each of

them by itself is a book of account. Learned counsel for the appellants/assessee urged that diaries recorded certain transactions and those

transactions were admitted by the assessee. The figures of the entries in the diaries tallied but with some inflation or additions. Hence, it is argued

that since the transactions were recorded and found correct, there was no concealment.

14. Learned counsel for the appellants relied upon the judgment in the case of The Commissioner of Income Tax, Punjab, Jammu and Kashmir

and Himachal Pradesh, Patiala Vs. Kartar Singh, and went on to contend that in the absence of any definition of ""books of account"" in the Act, the

diaries can constitute books of account, it need not be accurate or correct. Learned counsel for the appellants contended that the diaries, which

were seized, were regularly maintained as regular books of account which contained all the transactions entered into by the appellants. They

formed primary cash books containing particulars of all the transactions of the appellants. From this primary rough cash book, i.e., diaries, fair

account books were prepared. While recording these transactions from the rough cash book, namely, diaries to the fair cash book, certain

expenses were inflated but not a single transaction was missed out in the final cash book. In his submission, the rough cash book, i.e., diaries,

correctly recorded all the transaction and particulars thereof represented the true and correct picture of all the business transactions. In his

submission, the diaries, which accurately recorded all the transactions of the appellants, constituted the true books of account and could be

regarded as real cash book. In this view of the matter, he contended that the case of the appellants is squarely covered within Explanation 5 to

Section 271(1)(c) of the Act, as such entitled to claim benefit of this Explanation,

15. Learned counsel also sought to place reliance on Section 2(12A) of the Act, which defines ""books of account"" and urged that this definition is

brought on the statute book by way of clarification. It being clarificatory the same can be taken into account in the present appeals. Learned

counsel for the appellants submitted that the new definition of books of account is nothing but a recognition of the basic concept by which books of

account was understood. In his submission, all the lower authorities have erred in coming to the conclusion that the appellants' case did not fall

under the exception to Explanation 5 to Section 271(1)(c) of the Act. He thus prayed for setting aside the impugned order and deletion of penalty

imposed by the Assessing Officer and confirmed by the appellate authorities.

16. Per contra, learned senior counsel for the respondent, Shri R. V. Desai, at the outset, contends that the notices issued u/s 271(1)(c) did not

relate to any of the Explanations to the said section. In his submission, when the Income Tax Officer or the Appellate Assistant Commissioner

issues to an assessee a notice u/s 271, he makes the assessee aware that the provisions thereof are to be used against him. These provisions

include the Explanation. The assessee is, therefore, by virtue of the notice u/s 271 put to notice that if he does not prove, in the circumstances

stated in the Explanation, that his failure to return his correct income was not due to fraud or neglect, he shall be deemed to have concealed the

particulars of his income or furnished inaccurate particulars thereof and, consequently, be liable to penalty provided by that section. No express

invocation of the Explanation to Section 271 in the notice u/s 271 is necessary. He relies upon the apex court judgment in the case of M/s. K.P.

Madhusudhanan Vs. Commissioner of Income Tax, Cochin, wherein the apex court found it difficult to accept as correct the two judgments of

this court in the case of Commissioner of Income Tax Vs. P.M. Shah, followed in the case of Commissioner of Income Tax Vs. Dharamchand L.

Shah, . It is said (page 468): "... in the absence of invoking the Explanation specifically, the burden would remain on the Revenue to bring the

assessee's case within the mischief of the main provisions of Section 271(1)(c) of the Act.

17. Alternatively, Shri Desai contended that the books of account referred to in Clause (1) of Explanation 5 to Section 271(1)(c) of the Act means

the books of account maintained by the assessee meant to determine his income under the Income Tax Act. He further contended that books of

account means the account books maintained for the purposes of the Income Tax Act and not concealed account books, such as diaries in the

present case, surreptitiously maintained to record concealed and clandestine transactions not meant for the purposes of the Act. He, on this plank

of submission, tried to support the order of the authorities below and urged that by no stretch of imagination can the case of the appellants be said

to be within the sweep of Clause (1) of Explanation 5 to Section 271(1)(c) of the Act. He, therefore, prayed for dismissal of the appeals and

confirmation of the orders passed by the authorities below.

18. He tried to support the finding recorded by the Tribunal and contended that Explanation 5 to Section 271(1)(c) was not at all attracted in this

case, as no money, jewellery, bullion, was found during the search u/s 132 of the Act. He submitted that as a result of scrutiny of the seized

material an unaccounted income utilised for purchase of jewellery and investment of cash was worked out by the Assessing Officer as such

Explanation 5 did not attract.

Reframed question :

19. Having heard rival submissions, the question that needs consideration is : can the diaries, in the facts and circumstances of the case, be

regarded as books of account. What do you mean by books of account as understood in Explanation 5 of Section 271(1)(c) of the Act. On the

above factual matrix and legal backdrop, whether the diaries seized during the search operation u/s 132 could be regarded as books of account

maintained by the assessee as contemplated under Explanation 5 to Section 271(1)(c) of the Act for recording source of income ?

Statutory provisions :

20. Before we deal with the aforesaid question, raised on behalf of the appellants, it is appropriate to first consider the provisions applicable in the

present cases at hand.

271. (1) If the Assessing Officer or the Commissioner (Appeals) in the course of any proceedings under this Act, is satisfied that any person-- . . .

(c) has concealed the particulars of his income or furnished inaccurate particulars of such income, . . .

(iii) in the cases referred to in Clause (c), in addition to any tax payable by him, a sum which shall not be less than, but which shall not exceed three

times, the amount of tax sought to be evaded by reason of the concealment of particulars of his income or the furnishing of inaccurate particulars of

such income . . .

Explanation 5. --Where in the course of a search u/s 132, the assessee is found to be the owner of any money, bullion, jewellery or other valuable

article or thing (hereafter in this Explanation referred to as assets) and the assessee claims that such assets have been acquired by him by utilising

(wholly or in part) his income,--

(a) for any previous year which has ended before the date of the search, but the return of income for such year has not been furnished before the

said date or, where such return has been furnished before the said date, such income has not been declared therein ;
or

(b) for any previous year which is to end on or after the date of the search, then, notwithstanding that such income is declared by him in any return

of income furnished on or after the date of the search, he shall, for the purposes of imposition of a penalty under Clause (c) of Sub-section (1) of

this section, be deemed to have concealed the particulars of his income or furnished inaccurate particulars of such income, unless,--

(1) such income is, or the transactions resulting in such income are recorded,--

(i) in a case falling under Clause (a), before the date of the search; and

(ii) in a case falling under Clause (b), on or before such date, in the books of account, if any, maintained by him for any source of income or such

income is otherwise disclosed to the Chief Commissioner or Commissioner before the said date ; or

(2) he, in the course of the search, makes a statement under Sub-section (4) of Section 132 that any money, bullion, jewellery or other valuable

article or thing found in his possession or under his control, has been acquired out of his income which has not been disclosed so far in his return of

income to be furnished before the expiry of time specified in Sub-section (1) of Section 139, and also specifies in the statement the manner in

which such income has been derived and pays the tax, together with interest, if any, in respect of such income.

Legislative intention :

21. Prior to the insertion of Explanation 5 to Section 271 by the Taxation Laws (Amendment) Act, 1984, with effect from October 1, 1984, an

assessee, who is found to be the owner of any money, bullion, jewellery, etc., recovered during the course of search, was entitled to explain that

such assets were acquired by him by utilising his income relating to any previous year, whether it ended before the date of the search or is to end

on or before the date of the search. By doing so, the assessee could have escaped the liability of penalty u/s 271(1)(c).

22. In order to plug the aforesaid loop hole, Explanation 5 has been inserted by the Taxation Laws (Amendment) Act, 1984, with effect from

October 1, 1984. The newly inserted Explanation 5 enacts a deeming provision and has application to a situation where in the course of a search

u/s 132, the assessee is found to be the owner of any money, bullion, jewellery or other valuable articles or things ("assets" for short) and the

assessee claims that such assets have been acquired by him by utilising wholly or in part, his income for any previous year which has already ended

before the date of the search or which is to end on or after the date of the search. In such a situation, notwithstanding the fact that such income is

declared by him in any return of income furnished on or after the date of the search, he, for the purposes of Section 271(1)(c), is deemed to have

concealed the particulars of his income or furnished inaccurate particulars of such income except in case where such income, or the transaction

resulting in such income is recorded on or before the date of the search in the books of account, if any, maintained by him for any source of income

or such income is otherwise disclosed to the Commissioner before the date of the search.

23. In other words, as per existing Sub-clause (1) of Explanation 5 to Section 271(1)(c) of the Act, with which we are concerned, if at the time of

search, assets which were not recorded in the books of account are found, a taxpayer is liable to penalty for concealment even if he declares the

full value of those assets as his income in the return filed after the search. This provision is found to operate even in cases where the assessee has

no intention to fabricate any evidence and he includes in his return the income out of which such assets have been acquired. It has also been

provided that if an assessee in such case makes a statement during the course of search admitting that the assets found at his premises or under his

control had been acquired out of his income which have not been disclosed so far in his return of income to be furnished before the expiry of the

time prescribed in Clause (a) or (b) of Section 139(1) and specifies in the statement the manner in which such income has been derived and pays

the taxes that are due thereon, no penalty shall be leviable.

Consideration and findings

24. Having heard the parties, the facts reveal that penalty of concealment is levied u/s 271(1)(c) with respect to unsecured loans given, jewellery,

cash and purchase of properties. The Assessing Officer on the basis of scrutiny of the seized material worked out unaccounted income in the form

of unexplained jewellery and unexplained cash including unsecured loans given and on-money paid for acquiring immovable properties. The

exemption for the assessment year 1990-91 has been given to the assessee by the Assessing Officer by virtue of Clause (2) of Explanation 5 since

the return for that year had not become due with the result immunity from penalty u/s 271(1)(c) was granted to the assessee for the year 1990-91,

the year in which a raid took place but denied the same for earlier years. Since the Assessing Officer himself invoked Explanation 5 and granted

immunity to the assessee for the assessment year 1990-91, and the said order having become final and conclusive, for want of further challenge at

the instance of the Revenue, we do not think it necessary to dwell upon the question of applicability of Explanation 5 on the facts and in the

circumstances of the present case. Assuming it to be applicable even then, in our view, the appellants cannot succeed in these appeals for the

reasons recorded herein.

25. Explanation 5 to Section 271(1)(c) provides that if the assessee is found to be the owner of any money, bullion, jewellery or other valuable

articles or things during the course of search u/s 132 and if the assessee claims to have acquired such assets by utilising his income of the previous

year, for which returns are not filed, or discloses such income in the return of income filed after the date of the search, the assessee shall be

deemed to have concealed the particulars of such income. However, this Explanation itself reduces the rigour of the deemed concealment by

providing the following two exceptions :

(1)(a) such income or the transaction resulting in such income is found to be recorded in the books of account maintained by the assessee for any

source of income ; or

(b) such income is otherwise disclosed to the Commissioner before the date of search ; or

(2) the assessee during the course of the search makes a statement u/s 132(4) of the Act that any money, bullion, jewellery or other valuable

articles or things, etc., have been acquired by the assessee out of his income not disclosed so far in the return of income and also specifies the

manner in which such income was earned.

26. The above exceptions are alternative, and if the assessee is able to establish that his case is covered by any of the above exceptions, he would

be out of the clutches of Explanation 5 to Section 271(1)(c).

27. The appellants' case is that the diaries, which were seized, were regularly maintained in the regular course of business as regular books of

account, which contained all the transactions entered into by the appellants. It reflected a true state of accounts constituting the real cash book. As

such his case squarely falls within Explanation 5 to Section 271(1)(c) of the Act.

28. In order to appreciate the scope of Clause (1) to Explanation 5, it would be necessary to understand the words in which they are appearing

under the said Explanation. Before concentrating on the specific meaning thereof, in the light of the legislative intent behind Clause (1), let us see,

what do you mean by "books of account". If "books of account" is considered in isolation, then, it may mean books in which merchants, traders

and businessmen generally keep their accounts and are maintained for recording (a) all receipts and expenses with matters relating thereto; (b) all

sales and purchases; and (c) the assets and liabilities. They are the documents and ledgers which must be prepared and kept by the business entity

including the profit and loss account and the balance-sheet. In traditional terms, books means a collection of sheets of papers bound together with

the intention that such binding shall be permanent and papers used are kept collectively in one volume. It may also be assumed that it connotes the

intention that it should serve as a permanent record. At the same time, the term of account, i.e., to account, means to reckon, and it is difficult to

conceive of any accounting which does not involve either additions or subtractions or both of these operations of arithmetic. A book which

contains successive entries of items may be a good memorandum book; but until those entries are totalled or balanced, or both, as the case may

be, there is no reckoning and no accounts. A book which merely contains entries of items of which no account is made at any time, is not a "book

of account" in a commercial sense.

29. In different legislations the concept of books of account has been employed. One of such oldest legislation is the law of evidence. Section 34

refers to the words "entries in books of account". Section 34 has been interpreted by various High Courts including the apex court. The Supreme

Court in the recent judgment delivered in the case of Ishwar Dass Jain (Dead) Thr. Lrs. Vs. Sohan Lal (Dead) By Lrs., has observed as under

(headnote) :

Under Section 34 sanctity is attached in the law of evidence to books of account if the books are indeed "account books", i.e., in original if they

show, on their face, that they are kept in the "regular course of business".

30. So, the accounts u/s 34 means accounts which are maintained in the regular course of business.

31. The Income Tax legislation has been using the term "book" or "books of account" right from its inception. But, these terms are defined in the

Act for the first time by the Finance Act, 2001, with effect from June 1, 2001. Section 2(12A) defines the said terms to mean :

(12A) "books or books of account" includes ledgers, day-books, cash books, account books, and other books, whether kept in the written form

or as print-outs of data stored in a floppy, disc, tape or any other form of electromagnetic data storage device.

32. Then above definition appears to have been framed by the Legislature keeping in view the development of computer technology. If the newly

inserted definition of books of account inserted in the Income Tax Act is examined in contrast to the definition given u/s 34 of the Evidence Act, it

will be clear that the stringent requirements of Section 34 are not to be found in the said definition. Obviously, for the simple reason that the

purpose of both the legislations are different. So far as the cases at hand are concerned, they relate to the assessment years 1984-85 to 1988-89 ;

much prior to the period of introduction of the definition which was introduced for the first time under the Finance Act, 2001.

33. In order to appreciate the submissions keeping in view the facts of the present cases, one has to concentrate not only on the bare term "books

of account"" but also on the words in whose company the said term is appearing. The extracted sub-clause appearing hereinbelow will have to be

understood properly and appropriate meaning will have to be assigned keeping in mind the backdrop in which the concept of ""books of account"" is

referred to in Sub-clause (1) of Clause (b) of Explanation 5. The words used are :

such income is, or the transactions resulting in such income are recorded . . . in the books of account, if any, maintained by him for any source of

income . . . before the said date.

34. The term ""books of account"" referred to in Sub-clause (1) of Explanation 5 to Section 271(1)(c) means books of account which have been

maintained for determining any source of income. The term ""source of income"" as understood in the Income Tax Act is to identify or classify

income so as to determine under which head, out of the various heads of income referred to in Section 14 of the Act, it would fall for the purposes

of computation of the total income for charging Income Tax thereon. Thus, the term ""books of account"" referred to in this relevant sub-clause of

Explanation 5 would mean those books of account whose main object is to provide credible data and information to file the tax returns. A credible

accounting record provides the best foundation for filing returns of both direct and indirect taxes. Accounting is called a language of business. Its

aim is to communicate financial information about the financial results. This is not possible unless the main objectives of the books of account are to

maintain a record of business : to calculate profit earned or loss suffered during the period of time, to depict the financial position of the business ;

to portray the liquidity position ; to provide up to date information of assets and liabilities with a view to derive information so as to prepare a profit

and loss account and draw a balance-sheet to determine income and source thereof. Thus, the term ""books of account"" referred to in Explanation

5 must answer the above qualifications. It cannot be understood to mean compilation or collections of sheets in one volume. The books of account

referred to are those books of account which are maintained for the purposes of the Income Tax Act and not diaries which are maintained merely

as a man's private record ; prepared by him as may be in accordance with his pleasure or convenience to secretly record secret, unaccounted

clandestine transactions not meant for the purposes of the Income Tax Act, but with specific intention or desire on the part of the assessee to hide

or conceal income so as to avoid imposition of tax thereon.

35. The words in Explanation 5 ""books of account, if any, maintained by him for any source of income"" are important words signifying the

legislative intent embodied in the Explanation warranting grant of immunity from penalty. The legislative intent is to admit only those books of

account maintained by the assessee on his own behalf as by their very nature and circumstances are maintained for the purposes of drawing the

source of income. Therefore, when books of account are tendered for claiming the benefit of Explanation 5 to Section 271(1)(c) of the Act, it must

be shown to be a book, that book must be a book of account, and on the top of it that must be one maintained for the purposes of drawing the

source of income under the Income Tax Act. These essential requirements must be carefully observed while implementing tax legislation in the

country where secret and parallel accounts based on frauds and forgery are extremely common and responsibility of keeping and maintaining

accounts for the purposes of the tax legislation is honoured in the breach rather than the observance.

36. Now, turning to the facts of the cases in hand, private diaries may have been most regularly maintained, it may have been exhibiting record of

the factual facts, contemporaneously made but they were never maintained for the purposes of the Income Tax Act to draw the source of income

or for the computation of total income to offer income calculated therefrom for the purposes of taxation. Such books or diaries can hardly be

designed or accepted as books of account for the purposes of Explanation 5 of Section 271(1)(c) of the Act, so as to afford immunity from

penalty. None of the cases cited by the appellants were close to the facts found herein, hence no reference thereto in our opinion, is necessary.

37. The Tribunal was perfectly justified in upholding the levy of penalty u/s 271(1)(c) of the Act.

38. Accordingly, question of law reframed is answered in the negative, i.e., against the appellants/assesseees and in favour of the Revenue. In the

result, all the appeals are dismissed with no order as to costs.