

THE HON'BLE SRI JUSTICE C.V. NAGARJUNA REDDY  
AND  
THE HON'BLE SRI JUSTICE CHALLA KODANDA RAM

I.T.T.A. Nos.701 and 702 of 2016

DATED:23-02-2018

Between:

Pendurthi Chandrasekhar ... Appellant

And

The Deputy Commissioner of Income Tax  
Central Circle-11, Hyderabad ... Respondent

COUNSEL FOR THE APPELLANT: Mr. K. Vasanth Kumar

COUNSEL FOR THE RESPONDENT: Ms. M. Kiranmayee,  
Senior Standing  
Counsel for Income  
Tax Department

THE COURT MADE THE FOLLOWING:

**COMMON JUDGMENT:**

*(per the Hon'ble Sri Justice C.V. Nagarjuna Reddy)*

As the parties to these appeals are common and the subject matter is connected in both the cases, though not identical, we have heard both these appeals together and decided to dispose of the same by this common judgment.

2. The appellant (hereinafter referred to as “the assessee”) is an individual. A search under Section 132 of the Income Tax Act, 1961 (for short, “the Act”) in the group entities of M/s. Ambience Property Private Ltd., has taken place on 9.10.2007. As the assessee happens to be a Director of one of the group companies, namely, M/s. Dakshin Shelters Private Limited, a search took place at his residence also. The assessee has not filed any return of income prior to the search, as purportedly he did not have regular source of income. Consequently, proceedings under Section 153-A of the Act were initiated against the assessee. On receipt of the notice, he has filed his return of income for a total income of Rs.43,809/- for the assessment year 2006-07. The Assessing Officer (AO) did not accept the return. He has issued a notice proposing to make certain additions to the income of the assessee. The AO has eventually made additions to the income of the assessee. The additions in respect of the following items relating to the

assessment year 2006-2007, are the subject matter of dispute in these appeals.

- (i) Gift of Rs.73,00,000/- to the assessee by his maternal aunt Smt. Mikkilineni Nirmala.
- (ii) Unsecured loans of Rs.87,95,724/- from Mr. Dev Singh Palak.
- (iii) Addition of a loan of Rs.10,00,000/- received by the assessee as unsecured loan from Mr. J.V. Sudhakar, which was returned before the search by cheque.
- (iv) Interest income in respect of the amounts advanced by the assessee to M/s. Dakshin Shelters Pvt. Ltd. for which TDS was deducted and remitted to the tax authorities by the donee company
- (v) Unsecured loan of Rs.14,50,000/- given by the assessee's wife from out of the gift received from her father.

3. The assessee has filed an appeal before the Commissioner of Income Tax (Appeals)-I, Hyderabad [for brevity, "CIT(A)"], questioning the additions. The CIT(A), by order dt.30.11.2011 allowed the appeal of the assessee to the extent of item No.(v) addition of unsecured loan of Rs.14,50,000/- and dismissed the appeal in respect of other four items. Feeling aggrieved by the order of the CIT(A), the assessee has filed I.T.A. No.2120/H/11, and the Revenue has filed I.T.A. No.106/H/12 to the extent of the order of the CIT(A)

allowing the appeal in respect of item No.(v). By common order dt.22.3.2013, the Income Tax Appellate Tribunal, Hyderabad Bench 'A', Hyderabad, (hereinafter referred to as "the Tribunal") disposed of the appeals and cross-objections of the assessee, and the appeals of the Revenue for the assessment years 2005-06 to 2008-09. For the assessment year 2006-2007, it confirmed the order of the CIT(A) in respect of items Nos.(i) to (iv) and reversed the order in respect of item (v), in I.T.A. No.2120/H/11, and questioning the additions in respect of items (i) to (iv) the assessee filed I.T.T.A. No.701 of 2016, and he has filed I.T.T.A. No.702 of 2016 against the order of the Tribunal in allowing the appeal of the Revenue being I.T.A No.106/Hyd/12 in respect of item No.(v).

4. The substantial questions of law originally framed and those subsequently reframed in the appeals are as follows:

#### ITTA No.701/2016

Substantial questions of law originally framed:

#### "Item No.(i)

- (i) Whether on the facts and circumstances of the case, the Hon'ble Tribunal is right in upholding the addition under Section 68 of the IT Act, notwithstanding the fact that the Appellant/Assessee has discharged his onus of proof regarding the gift by furnishing all the materials required for establishing the genuineness of the gift?
- (ii) On the facts and circumstances of the case, whether the Hon'ble Tribunal is justified in adopting the theory of 'occasion' in respect of the gift received by the

Appellant/Assessee, which is regulated by the provisions of Proviso (a) of Section 56(1)(v) of the IT Act, 1961, under which in case of specified relatives inter se, no 'occasion' is required to make a gift irrespective of its quantum?

- (iii) Whether the findings of the Hon'ble Tribunal are perverse and bad in law due to non-consideration of relevant factors and instead basing it on surmises, conjectures and suspicion and by discarding the evidence and the reasons and explanations adduced by the Appellant/Assessee for the gift and proving the source of funds for making the gift and despite the clinching evidence to establish the gift, the test of 'occasion' for gift, which is quite irrelevant and strikes at the root of the concept of gifts as understood in law was imposed, which thereby stand vitiated?

Item No.(ii)

- (i) Whether the Tribunal has committed a serious error of law in brushing aside clinching evidence in the form of documents evidencing the loan transaction by means of cryptic observation that the Appellant/Assessee has not discharged burden of proof?
- (ii) Whether finding of the Tribunal is vitiated is evident from the fact that the Tribunal refers to 'donor and gift' which do not exist here?
- (iii) Whether the two reasons given by the First Appellate Authority and relied on by the Tribunal, viz, the evidence by way of documents filed, does not have any evidentiary value in the absence of any authentication and secondly, such huge amounts of loan could not have been given by a friend residing in the UK without any return are either irrelevant or based on surmises, conjectures and suspicion?

Item No.(iii)

“The Assessing Officer having independently called for the bank account statements of Mr. J.V. Sudhakar and having compared it with the bank account statements of the Appellant/Assessee and having found that the loan transaction was genuine and the repayment of the loan having also been made in less than four months through bank transfer, all these transactions having taken place long before the search, was the Assessing Officer right in drawing a hasty conclusion against the veracity of the loan due to the mere non-appearance of Mr. J.V. Sudhakar by the summons issued to him by overlooking the fact that Mr. J.V. Sudhakar was a person of substantial means and had the sources to give the loan, without re-issuing the summons to him, thereby, vitiating the finding and order against the Appellant/Assessee and therefore causing a miscarriage of justice to the Appellant/Assessee?

Item No.(iv)

- (i) Whether the Hon'ble Tribunal was justified in law in upholding the addition of interest not received by the Appellant/Assessee only on the reasoning that the Appellant/Assessee had claimed credit towards TDS on the basis of the certificate sent by the loanee company?
- (ii) Whether the Appellant/Assessee who was consistently following the cash system of accounting would be required to account for such unreceived interest merely because the income stood credited to his account in the book of the loanee company, which has been following the mercantile system of accounting?
- (iii) Whether the reasoning of the Tribunal at Para 71 that claiming of credit towards TDS and claiming of deduction of interest shall go together and there could not be dual method for the same income is sustainable in law especially having referred to the provision contained in Section 145 of the I.T. Act and the inequitable consequences that flow?
- (iv) Whether the factum of adjusting TDS against the tax payable by Appellant/Assessee would ipso facto convert the income not at all received by the Appellant/Assessee as taxable income for the relevant year?
- (v) Whether on the facts and circumstances of the case, the Hon'ble Tribunal is justified in upholding the addition towards interest income by observing that the Appellant/Assessee claimed credit towards TDS on the disputed interest income and for other portion of interest the Appellant/Assessee is following cash system of accounting?
- (vi) Whether the impugned order is not perverse as the Hon'ble Tribunal has failed to consider the materials on record and considered irrelevant materials in arriving in its decision?"

**Reframed substantial questions of law:**

1. "Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal while confirming the addition of Rs.73,00,000 as unexplained credit under Section 68 of the Act, is right in law in holding that there should be sufficient reasons for receiving gifts though it is from mother's sister and the gift is covered by the provisions of Section 56 of the Act?
2. Whether on the facts and in the circumstances of the case, the decision of the Income Tax Appellate Tribunal is perverse and without application of mind in confirming the addition of Rs.87.95 lakhs received as loan from Mr. Devsingh Palak, on the ground that the burden of proof is on the assessee to establish that the donor has means and the gift was genuine though it is a loan and burden is discharged by filing all required documents?

3. Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal is right in law in ignoring the reference made by the Assessing Officer to the Foreign Tax Division of the Central Board of Direct Taxes requesting to verify the genuineness of the amounts received from UK and confirming the addition though no adverse communication is received as per records?
4. Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal is right in law in confirming the addition of Rs.10,00,000 being loan received and repaid from one Mr. J.V. Sudhakar on the ground that his identity is not proved though the transaction is through bank and assessee discharged his burden?
5. Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal is right in law in upholding the conclusion of the Assessing Officer and the learned Commissioner of Income Tax (Appeals) that undisclosed income has been brought in the form of gifts in spite of the fact that there was no income earning activity to the assessee?
6. Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal is right in law in holding that the assessee has to discharge his onus though the assessee has complied with the provisions of law?
7. Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal while confirming the addition of Rs.3,05,713 as interest income on mere ground of claiming credit for TDS on entire amount in utter disregard to the provisions of Sec. 145 of the Act and method of accounting followed by the assessee?"

ITTA No.702/2016

Substantial questions of law originally framed:

- (a) "Whether the Tribunal was legally justified in treating the loan given by the wife of the Appellant/Assessee as unexplained cash credit on the two grounds, viz, (1) that the credit received by the Appellant/Assessee cannot be said to be genuine unless there is evidence to establish that the wife is having sources of income and that her own income is not much, and; (2) it is "very easy to make self-serving gift letter" and relying on it;
- (b) In making the above observations, whether the Hon'ble Tribunal has committed an error of law in as much as the Tribunal overlooked the material on record, establishing the source of her funds and secondly, found fault with the confirmation of gifts letter, by merely characterising the same as "self-serving"?
- (c) Whether under the facts and circumstances of the case, the Hon'ble Tribunal was justified in reversing the Order of the Commissioner of Income Tax (Appeals) without evaluating and

appreciating the materials on record furnished by the Appellant/Assessee to substantiate the genuineness of the transactions?

- (d) Whether under the facts and circumstances of the case, the direction given by the Commissioner of Income Tax (Appeals) to the Assessing Officer to take steps to assess the credit amounts in the hands of the lender?
- (e) In view of the reference to FTD of CBDT having not brought out any adverse finding against the Appellant/Assessee, is the order of the Hon'ble Tribunal liable to be struck down by drawing adverse inference against the revenue under illustration (g) of Section 114 of the IT Act."

#### Reframed substantial questions of law:

1. Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal while reversing the decision of the Commissioner of Income Tax (Appeals) and confirming the addition of Rs.14,50,000 received as loan from wife Smt. P. Shanti Chowdary as unexplained credit under section 68 of the Act, is right in law in holding that genuineness of the transaction is not proved in spite of substantial evidence on record?
2. Whether on the facts and in the circumstances of the case, the decision of the Income Tax Appellate Tribunal is perverse and without application of mind in confirming the addition of Rs.14,50,000/- received as loan from Smt. P. Shanti Chowdary?
3. Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal is right in law in ignoring the reference made by the Assessing Officer to the Foreign Tax Division of the Central Board of Direct Taxes requesting to verify the genuineness of the amounts received from UK and confirming the addition though no adverse communication is received as per records?
4. Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal is right in law in upholding the conclusion of the Assessing Officer and the learned Commissioner of Income Tax (Appeals) that undisclosed income has been brought in the form of gifts in spite of the fact that there was no income earning activity to the assessee?"
5. At the hearing, Mr. K. Vasanth Kumar, learned counsel for the assessee, submitted that the CIT(A) as well as the Tribunal fell into serious error in treating the gift from the assessee's aunt as unexplained credit under Section 68 of the

Act on unsustainable inferences and unwarranted presumptions. That the reasoning of the Tribunal that there was no occasion for the assessee to accept the gift is in the teeth of Section 56(2)(v) of the Act introduced with effect from 01.4.2005 envisaging that for a relative no occasion is needed for making a gift. The learned counsel further submitted that for drawing a conclusion of undisclosed income, the authority must find a source for the assessee and that no such source has been detected. In support of his submissions, the learned counsel placed reliance on the judgment in **C.I.T. v. P. Mohanakala**<sup>1</sup>. The learned counsel further submitted that the maternal aunt of the assessee has gifted the amount received from her daughter sent from the United States of America as evident from the bank statements including the US bank statements and confirmation issued by the bank. That the said amount was received from abroad and that the AO has made the addition by stating that the statement of the assessee that his mother and father looked after her and that as she has no male child she treated him as her son, is false, which is wholly unsustainable.

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<sup>1</sup> (2007) 291 ITR 278

6. As regards item No.(ii), i.e., loan received from Mr. Dev Singh Palak, the learned counsel submitted that during the financial year 2005-06 the assessee has received a loan of Rs.87,95,000/- from one of his family friends, Mr. Dev Singh Palak, a resident of U.K., that out of the said sum, Rs.47,45,724/- was received from U.K. and the balance was received from Punjab in the form of demand drafts. That during the course of assessment proceedings, the assessee submitted confirmation letters from Mr. Dev Singh Palak, the U.K. company, which transferred the amount, the company's financial statements, confirmation of the drafts and copies of sale of lands in Punjab. The AO, submitted the counsel, however, held that the loan is not proved and that he has further held that the signature of the person in the confirmation demonstrates that the person is not a man of means. The learned counsel submitted that such a reasoning of the AO, as confirmed by both the appellate authorities, cannot stand the scrutiny of the Court.

7. With regard to item No.(iii), the learned counsel submitted that during the financial year 2005-06, the assessee received Rs.10,00,000/- as loan from one J.V. Sudhakar on 21.3.2006 and the same was repaid on 5.7.2006 by bank

transfer. That during the course of the assessment proceedings as the said Sudhakar was not available, he could not appear before the AO. That the AO obtained bank statement from the bank which proves the version of the assessee and that in spite of the same, the AO has added the amount as unexplained credit on the ground that identity of the creditor was not proved. The learned counsel submitted that the reasoning of the AO as confirmed by both the appellate fora is not sustainable, as the very bank statement obtained by the AO proves the identity of the creditor and his creditworthiness.

8. As regards item No.(iv) - the addition of Rs.3,05,713/-, the learned counsel submitted that the assessee advanced loan to the company, by name, M/s. Dakshin Shelters Private Limited, on various dates. That the company though credited interest in its books of account and deducted tax at source, it has never paid interest to the assessee. That the assessee followed the cash system of accounting and admitted the tax deducted at source as income and claimed the credit for TDS as the same was admitted as income. That during the course of the assessment proceedings, the AO was informed that the interest income in its entirety is not admitted as the assessee is following cash system of accounting. The AO however held

that as the basis of charge is Section 5 of the Act, interest income is taxable totally ignoring Section 145 of the Act which mandates admission of income on the basis of accounting method. The learned counsel argued that if the company has followed the accounting method and debited the amount in its accounts as being paid to the assessee and deducted tax at source, as for the assessee as he was following only cash system he has not included the amount under income as he has not received the same during that financial year. That even the Central Board of Direct Taxes while issuing clarification on the recently introduced provisions of Income Computation and Disclosure Standard, has recognised this method and gave clarification in this regard. In this context, the learned counsel has referred to Section 199 of the Act which envisages that credit shall be given in the year when income is assessable, that the assessee admitted income to the extent of TDS on receipt basis/cash basis and that once the income to this extent is admitted there is no error in claiming credit for TDS. The learned counsel further submitted that the AO should have at best directed to restrict the claim of TDS in proportion to the income admitted and to allow the balance in the year in which the interest income is admitted on receipt basis. That the

assessee has admitted entire interest income in the assessment year 2012-13, as in the previous year relevant to that assessment year, the deposit was converted into shares by the said company. The learned counsel accordingly submitted that the order of the AO, as confirmed by the CIT (A) and the Tribunal suffers from non-application of mind and is contrary to law.

9. As for item No.(v), which is the subject matter of ITA No.702 of 2016, the learned counsel submitted that during the financial year 2005-06 the assessee received loan of Rs.14,50,000/- from his wife, Smt. P. Shanti Chowdhary, by way of transfer from her bank account to the assessee's bank account on three dates, that during the course of assessment proceedings the assessee filed confirmation letter along with bank statement, details of gifts received by her from her father and that of foreign remittances to her account, and that the loan was given from out of the gifts received by his wife. The learned counsel also submitted that the petitioner's wife is the only daughter to her parents, who are U.K. citizens and also Doctors, that in proof of transferring the money to the assessee's wife by her father, relevant bank statements were filed. That the AO has not accepted the material and made the addition as unexplained credit under Section 68 of the Act and

that the CIT(A), however, has allowed the assessee's appeal, but the Tribunal on an erroneous view of the matter, reversed the said order of the CIT(A).

10. Ms. M. Kiranmayee, learned Senior Standing Counsel for the Income Tax Department, opposed the above submissions and commended the correctness of the decision of the AO and the two appellate fora in respect of the order challenged in ITTA No.701 of 2016, and the decision of the Tribunal reversing the order of the CIT(A) challenged in ITTA No.702 of 2016.

11. We have carefully considered the respective submissions of the learned counsel for both the parties with reference to the record.

12. With regard to item No.(i), the learned counsel placed heavy reliance on the following material which was produced before the AO. (i) The confirmation letter dt. Nil, given by Smt. Mikkilineni Nirmala, maternal aunt of the assessee, that she has transferred voluntarily a sum of Rs.73,00,000/- from her SB Account No.737010068905, ING Vysya Bank, Banjara Hills, Hyderabad, on 16.07.2005 to the SB Account No.737010054632 of the same bank belonging to the assessee. (ii) The copy of the statement of account of said Nirmala,

issued by the ING Vysya Bank, on 18.3.2010, showing credit of Rs.73,23,152/- in her account on 08.07.2005 and debit of Rs.73,00,000/- on 16.7.2005 and transfer to the SB Account 54632 belonging to the assessee. (iii) The copy of the statement showing Remittance (Purchase) of \$1,68,200 showing that Sudha R Ravoori has remitted the aforesaid sum to ING Vysya Bank to the account of Nirmala Mikkilineni, via Abn Amro, New York, and crediting of the said amount to the account of said Nirmala Mikkilineni. (iv) The copy of the statement of account No. 737010054632 standing in the name of the assessee for the period from 01.04.2005 to 31.03.2006, showing credit of sum of Rs.73,00,000/- on 16.7.2005. (v) The copies of Passport of R. Sudha Rani, daughter of Smt. Nirmala Mikkilineni. (vi) The copy of the statement of account of Bank One of USA, standing in the name of Sudha Rani Ravoori for the period from 27.6.2005 to 20.7.2005 *inter alia* showing electronic withdrawals of \$1,68,200.00 from her bank account, to the account of Nirmala Mikkilineni, via., Abn Amro, on 05.7.2005.

13. In his order, the CIT(A) has mainly relied upon the circumstance that the assessee failed to show any occasion for which such huge amount could have been given as gift, that too

by maternal aunt, and that it is very odd to note that the entire amount received from her daughter has been diverted to the assessee as a gift without any consideration. The Tribunal placing reliance on the judgment in **Tirath Ram Gupta v. C.I.T.**<sup>2</sup>, **Jaspal Singh v. C.I.T.**<sup>3</sup>, held that unless the identity of the donor, his creditworthiness, relationship with the donee and the occasion are proved, the plea of gift cannot be accepted.

14. In this context, the provisions of Section 56(1) and (2)(v), and Section 68 of the Act are relevant which read as under:

**“Income from other sources.**

**“56.(1).** Income of every kind which is not to be excluded from the total income under this Act shall be chargeable to income-tax under the head “Income from other sources” if it is not chargeable to income-tax under any of the heads specified in section 14, items A to E.

(2) In particular, and without prejudice to the generality of the provisions of sub-section (1), the following incomes, shall be chargeable to income-tax under the head “Income from other sources”, namely: -

(i) to (iv)...

(v) where any sum of money exceeding twenty-five thousand rupees is received without consideration by an individual or a Hindu undivided family from any person on or after the 1<sup>st</sup> day of September, 2004 but before the 1<sup>st</sup> day of April, 2006, the whole of such sum:

**Provided** that this clause shall not apply to any sum of money received-

- (a) from any relative; or
- (b) on the occasion of the marriage of the individual; or
- (c) under a will or by way of inheritance; or
- (d) in contemplation of death of the payer; or
- (e) from any local authority as defined in the Explanation to clause (20) of section 10; or

<sup>2</sup> 304 ITR 145 (P&H)

<sup>3</sup> 290 ITR 306 (P&H)

- (f) from any fund or foundation or university or other educational institution or hospital or other medical institution or any trust or institution referred to in clause (23C) of section 10; or
- (g) from any trust or institution registered under section 12AA.

Explanation.- For the purposes of this clause, “relative” means –

- (i) spouse of the individual;
- (ii) brother or sister of the individual;
- (iii) brother or sister of the spouse of the individual;
- (iv) brother or sister of either of the parents of the individual;
- (v) any lineal ascendant or descendant of the individual;
- (vi) any lineal ascendant or descendant of the spouse of the individual;
- (vii) spouse of the person referred to in clauses (ii) to (vi)”

#### **Cash credits.**

**68.** Where any sum is found credited in the books of an assessee maintained for any previous year, and the assessee offers no explanation about the nature and source thereof or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the sum so credited may be charged to income-tax as the income of the assessee of that previous year:

**Provided** that where the assessee is a company (not being a company in which the public are substantially interested), and the sum so credited consists of share application money, share capital, share premium or any such amount by whatever name called, any explanation offered by such assessee-company shall be deemed to be not satisfactory, unless –

- (a) the person, being a resident in whose name such credit is recorded in the books of such company also offers an explanation about the nature and source of such sum so credited; and
- (b) such explanation in the opinion of the Assessing Officer aforesaid has been found to be satisfactory:

**Provided further** that nothing contained in the first proviso shall apply if the person, in whose name the sum referred to therein is recorded, is a venture capital fund or a venture capital company as referred to in clause (23FB) of section 10.”

15. Section 56(2)(v) was inserted by the Finance Act, 2005 with effect from 1.4.2005. The relevant assessment year is 2005-2006. As rightly submitted by the learned counsel for the

assessee, for accepting a gift from a relative, no occasion need be proved. As could be seen from the language of sub-clauses (a) and (b) of clause (v) of sub-section (2) of Section 56, while under clause (a) which deals with a gift from any relative no occasion is envisaged, clause (b) dealing with money received from any other person, specifies the occasion of marriage. The explanation to the said provision defined 'relative', as persons including brother or sister of either of the parents of the individual. All the three fora below failed to refer to and discuss this pivotal provision.

16. Section 68 of the Act which deals with cash credits laid down that where any sum is found credited in the books of an assessee maintained for any previous year, and the assessee offers no explanation about the nature and source thereof or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the sum so credited may be charged to income-tax as the income of the assessee of that previous year. This provision could be pressed into service where the assessee offers no explanation. In the instant case, Section 68 is not attracted for the reason that the assessee has offered an explanation supported by uncontroverted material showing transfer of the amount from the daughter of the

assessee's maternal aunt and the latter in turn transferring the money to the assessee.

17. Section 68 of the Act fell for interpretation of the Supreme Court in many a judgment. In **Sumati Dayal v. C.I.T.**<sup>4</sup>, the Supreme Court held as under:

“In all cases in which a receipt is sought to be taxed as income, the burden lies on the Department to prove that it is within the taxing provision and if a receipt is in the nature of income, ‘the burden of proving that it is not taxable because it falls within exemption provided by the Act lies upon the assessee’ [See *Parimisetti Seetharamamma v. C.I.T.* : (1965) 57 ITR 532]. But, in view of s. 68 of the Act, where any sum is found credited in the books of the assessee for any previous year the same may be charged to income-tax as the income of the assessee of that previous year if the explanation offered by the assessee about the nature and source thereof is, in the opinion of the Assessing Officer, not satisfactory. In such a case there is, *prima facie*, evidence against the assessee, viz., the receipt of money, and if he fails to rebut, the said evidence being unrebutted, can be used against him by holding that it was a receipt of an income nature.”

18. On reviewing the case law on the subject, the Supreme Court in **P. Mohanakala** (1 *supra*) held in paragraph 12 as under:

“12. The question is what is the true nature and scope of Section 68 of the Act? When and in what circumstances Section 68 of the Act would come into play? That a bare reading of Section 68 suggests that there has to be credit of amounts in the books maintained by an assessee; such credit has to be of a sum during the previous year; and the assessee offers no explanation about the nature and source of such credit found in the books; or the explanation offered by the assessee in the opinion of the Assessing Officer is not satisfactory, it is only then the sum so credited may be charged to income-tax as the income of the assessee of that previous year. The expression "the assessee offers no explanation" means where the assessee offers no proper, reasonable and acceptable explanation as regards the sums found credited in the books maintained by the assessee. It is true the

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<sup>4</sup> 1995 Supp. (2) SCC 453

opinion of the Assessing Officer for not accepting the explanation offered by the assessee as not satisfactory is required to be based on proper appreciation of material and other attending circumstances available on record. The opinion of the Assessing Officer is required to be formed objectively with reference to the material available on record. Application of mind is the sine qua non for forming the opinion.”

19. A Division Bench of this Court in **R.B. Mittal v. Commissioner of Income Tax**<sup>5</sup>, after copious reference to the case law, observed as under:

“From the above discussion of the case law on the point what transpires is that the assessee, in order to discharge the onus cast on him under s. 68 of the Act, has to establish not only the identity of his creditors and confirmation of the credits but also the capacity of the creditors to advance money as well as the genuineness of the transactions.”

20. In the instant case, though the AO has stated as a general proposition of law that creditworthiness and identity of the donor and the genuineness of the gift, apart from establishing the occasion are relevant, no specific finding was rendered by him that the assessee has not established the identity and relationship of the donor with him. The AO has primarily misdirected himself in thinking that the main ingredient for a valid gift is proof of existence of occasion. This demonstrably is a flawed reason as the same is in the teeth of Section 56(2)(v(a) of the Act, as discussed above.

21. The further observation of the AO that the assessee appeared to have opened the bank account only for the

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<sup>5</sup> (2000) 246 ITR 283

purpose of receiving cash in the guise of a gift, is also flimsy. When the donor herself has given a confirmation letter clearly stating therein that she has transferred the amount of Rs.73,00,000/- to the account of the assessee and further declaring that she gave the said gift out of her natural love and affection towards her nephew, the AO ought not to have entertained further doubts. If for facilitating receipt of a gift the assessee has opened an account, we do not find anything wrong in that. In our opinion, the whole approach of the AO is wholly perverse which cannot be sustained. Equally, the reasons assigned by the two appellate bodies confirming the order of the AO are also perverse.

22. The findings of the CIT(A) that gifts are traditional in nature, that they are given in functions like marriages etc., that there was no such occasion warranting receipt of gift from Nirmala to the assessee, and that it is very odd to note that the entire amount received from her daughter has been diverted to the assessee as a gift without any consideration, look to us to be empty sermons as the CIT (A) evidently judged the conduct of the parties from his personal perception, which is wholly impermissible.

23. When the Act itself does not envisage any occasion for a relative to give a gift, it is well-nigh impermissible for any authority and even for that matter for the Court to import the concept of occasion and develop a theory based on such concept. The donor being no other than the assessee's own maternal aunt, is a 'relative' as defined under the explanation to Section 56(2)(v) of the Act and in the light of the plea of the assessee that she was brought up by the assessee's parents, and her daughters having already been married off and in a well-to-do position, it cannot be said that such a gift falls beyond "human probability" test as quite often applied by the Courts. Hence, it is not permissible for the AO to judge the conduct of the donor sitting in his arm chair.

24. As held by the Supreme Court in **P. Mohanakala** (1 supra) when an explanation is offered by the assessee for the cash receipt, the AO is required to form an opinion objectively based on proper appreciation of material and application of mind which is a *sine qua non* for forming the opinion. Such approach, in our opinion, is utterly lacking in the order of the AO. When the documents filed by the assessee referred to above clinchingly establish that the donor's daughter, an NRI with independent source of income, transferred the money

from her bank account to her mother's account and the latter in turn has transferred the money to the assessee, there is no justification for the AO to doubt the authenticity of these documents. If he had any such doubts, he should have referred those documents to the ING Vysya Bank, whose statements of account were filed by the assessee, to get their authenticity confirmed. No such effort was made by the AO.

25. The judgments in **Tirath Ram Gupta** (2 supra) and **Jaspal Singh** (3 supra) turn on their own facts. In **Tirath Ram Gupta** (2 supra) the Punjab & Haryana High Court held that the ingredients, namely, identification of the donor, his means and the genuineness of the gift were established, and the relevant assessment year therein being 1997-1998, which is much prior to the insertion of clause (v) of sub-section (2) of Section 56 of the Act, a finding was therefore rendered that the assessee has failed to prove the occasion for accepting the gift. Similarly, the judgment in **Jaspal Singh** (3 supra) relates to the assessment year 1998-99. The Tribunal failed to take notice of the distinction between the facts of the said cases and the present case which arose after the amendment to Section 56 of the Act.

26. As regards item No.(ii), it is the pleaded case of the assessee that during the financial year 2005-06, he has received loan of Rs.87,95,000/- from one of his family friends by name Mr. Dev Singh Palak, who is a resident of U.K., that out of the said amount, an amount of Rs.47,45,724 was received from U.K. and the balance amount was received from Punjab in the form of demand drafts. During the course of assessment proceedings, the assessee submitted confirmation letters from Mr. Dev Singh Palak, the U.K. company which transferred the amount, the company's financial statements, confirmation for the drafts and evidence of sale of lands in Punjab. The AO has however held that the loan is not proved and further held that the signature of the person in the confirmation demonstrates that the person is not of a man of means. The CIT(A) and the Tribunal confirmed the order of the AO.

27. The learned counsel for the assessee argued that the Tribunal in its order fell into an error in proceeding on the premise that the receipt of the amount by the assessee was by way of a gift, whereas it was only a loan and that on this assumption the Tribunal held that the assessee has not proved the means of the donor and that the gift was genuine. It is further argued that the AO has made reference to the CBDT

Cell on Foreign Transactions for verification of the genuineness of the transaction, but no report was received even till the date of disposal of the appeal by the Tribunal. That the loan transaction is genuine one is supported by several documents filed by the appellant before the AO.

28. We have carefully perused the copies of the documents filed by the assessee in these appeals. In its letter dt.7.10.2009 a company by name Eurox UK confirmed to the AO that on 25.5.2005 Future Garments Limited transferred the sum of £60,000 to the ING Vysya Bank Limited in Hyderabad, India, to be credited to account number 737010054632, held by the assessee and that these funds were transferred on behalf of Mr. Dev Singh of 209, Lordswood Road, Harborne, Birmingham, B17, 8QP, England and payment being in respect of a liability in the company accounts in favour of Mr. Dev Singh. Even Mr. Dev Singh addressed letter dt.2.6.2009 from UK from the same address as found in Eurox UK letter dt.7.10.2009 to the AO, wherein he has confirmed that he has given Rs.87,95,724/- towards interest free unsecured loan to the assessee on various dates commencing from 27.5.2005 to 19.7.2005, that he has given the said amount out of his income/savings and that he is a British Citizen and a business man. It is evident from the said

letter that on 27.5.2005 a sum of Rs.47,45,724/- was sent to the assessee by wire transfer. In order to prove that fact, the assessee has filed a copy of inward remittance (purchase) dt.27.5.2005 generated by the ING Vysya Bank Limited, Secunderabad, showing that Future Garments Limited remitted a sum of £60,000 equivalent to Rs.47,46,000/- at the rate of Rs.79.1000 per pound. The assessee also produced Passport and a copy of electricity bill, showing permanent address of Mr. Dev Singh Palak in UK and also that he is a British citizen. A copy of the independent audit report in respect of Future Garments Limited, was also filed to show that Davinder Kaur Palak, Hardip Singh Palak, Kuldip Singh Palak and Manjir Kaur Palak have 3,125/- shares each in the said company. Mr. Dev Singh Palak has sent a notarized affidavit, wherein he has *inter alia* stated as under:

#### AFFIDAVIT

I, Dev Singh Palak, S/o. Gulzara Singh, aged about 69 years, Resident of 209, Lordswod Road, Harborne, Birmingham B17, West Midlands, United Kingdom, Occupation: Retired, do hereby affirm and state that.

1. I am a citizen of United Kingdom with British Passport No.GBR 456123613.
2. I am having two sons by name Kuldip Singh and Hardip Singh who are also residents of Birmingham, UK.
3. We are having business concerns in the name of M/s. Aqua Holdings Limited and M/s. Future Garments Limited shareholding total held by me and my two sons Kuldip Singh and Hardip Singh and our respective wives. Palak is our surname. EUROX is the Branding name of M/s.Future Garments Limited

registered in UK with Registration number 2690536, having registered office at Aqua house, Buttress Way, Smethwick, West Midlands, B663DL.

4. M/s. Aqua Holdings Limited is the wholly owned holding company of M/s. Future Garments Ltd.
5. I was born in Malupota village in Punjab, India, in the year 1940 and shifted to United Kingdom (UK) in the year 1973 and since then I am staying in UK working in the family business.
6. Myself and my family members are having agriculture lands in Punjab. My brother-in-law Mr. Avatar Singh is looking after these agriculture lands on our behalf. We visit our village and agriculture lands occasionally as and when required.
7. Sri P. Chandra Sekhar is well known to me while he is staying in UK with his father-in-law, in the same locality. He is a family friend for more than 15 years to me and my sons, Kuldip & Hardip.
8. I have given the following unsecured loan to Sri P. Chandra Sekhar.

| Date      | Nature of Transaction | Mode of Transaction | Amount Rs.                                 |
|-----------|-----------------------|---------------------|--------------------------------------------|
| 25.5.2005 | Unsecured loan        | Wire Transfer       | £ 60,000<br>Equivalent<br>INR<br>47,45,724 |
| 19.7.2005 | Unsecured loan        | Demand Drafts       | 40,50,000                                  |
| Total     |                       |                     | 87,95,724                                  |

1. The amount of £ 60,000 was paid from the amounts due to me by the company M/s. Future Garments Ltd. and as explained above this amount was transferred by my son Kuldip Palak on the direction given by me as he is the director of the company, M/s. Future Garments Limited.
2. Amount of Rs.40,50,000 was sent by way of five demand drafts in the name of Sri P. Chandra Sekhar. This amount was sent by my brother-in-law Mr. Avatar Singh on the basis of my instructions to him. This amount consists of the sale proceeds of agricultural lands which are in name of my sons Kuldip and Hardip and sold for a sum of Rs.36,75,000/- vide sale deed No.3991 dated 24/6/2005 and the balance amount from the monies due to my family from Mr. Avatar Singh.

This affidavit I am giving with free will and consent and with full knowledge of contents in this affidavit.”

Deponent

Dev Singh Palak”

The assessee has also filed copies of the sale deeds executed by Kuldip Singh and Hardip Singh Palak, sons of Mr. Dev Singh Palak, conveying agricultural lands for consideration of Rs.40,50,000, and proof of sending that amount to the assessee by way of demand drafts, by Avatar Singh, brother-in-law of Dev Singh Palak living in Punjab. Here again the CIT(A) has adopted a fractured reasoning by imposing his personal views on Mr Dev Singh Palak as could be seen from the following observations.

“No shareholder can maintain any account in the company in the first place. Even the contents of letter of Future Garments reveals that the amount given represents liability of Mr. Dev Singh. It is totally uncommon to obtain loan from a company and pass on the same to Indian resident as a loan without any interest on such loan. It is against the human probability of any friend to advance such substantial sums without any return on such sums.”

29. Letter dt.07.10.2009 of Eurox UK reads as under:

“e u r o x UK

Deputy Commissioner of Income Tax  
Central Circle 2  
Hyderabad, A.P  
INDIA

Date: 7<sup>th</sup> October, 2009

Subject: Funds transfer of \$60,000 to Mr. Chandra Sekhar,  
Pendurthi on 25<sup>th</sup> May 2005.

Dear Sir,

Please be advised that on 25<sup>th</sup> May, 2005, Future Garments Limited transferred the sum of £60,000 (Sixty Thousand Pounds only), to the ING Vysya Bank Ltd. in Hyderabad, India, to be credited to account number 737010054632, held in the name of Mr. Chandra Sekhar Pendurthi..

'These funds were transferred on behalf of Mr. Dev Singh of 209 Lordswood Road, Harborne, Birmingham, B17 8 QP, England, payment being in respect of a liability in the Company Accounts in favour of Mr. Singh.'

Yours faithfully,

Peter GW Round A.C.M.A.  
Finance Director"

In our opinion, the CIT(A) has misread the transactions. If we carefully read the letter dt.7.10.2009 of Eurox UK, as reproduced above, it is clear that M/s.Future Garments Limited transferred £60,000 on behalf of Mr. Dev Singh Palak to be credited to the assessee's account. In his affidavit filed by Dev Singh Palak, it is clearly stated that the sum of £60,000 was transferred on behalf of Dev Singh Palak "in respect of a liability in the Company's Accounts in favour of Mr. Singh". It thus appears that the company owed money to Dev Singh Palak and not vice versa and the said amount was transferred by the company to the account of the assessee. However, the CIT(A) was under the wrong assumption that Mr. Dev Singh Palak has obtained loan from the company. On such erroneous premise, he observed that no one would lend interest free loan from out of borrowed money. On what terms a person advances loan to another person depends upon the relationship and the implied understanding between them. While in his letter dt.2.6.2009 Dev Singh Palak has confirmed that he has

sent the amount towards interest free unsecured loan to the assessee, there is no reason to infer that Dev Singh Palak has not expected any return from the assessee. It could well be that the assessee may have intended to invest the amount profitably and share the proceeds. At the time of scrutiny there was no obligation for the assessee to explain his future plans as to how he intends to utilise the loans he received, as it will be his responsibility to account for the gains if any made on such investments, as and when they are made. Similarly, the finding of the CIT (A) that “no person would sell the ancestral properties at the village and pass on the sale proceeds in entirety to a friend in India without any consideration or yield on such amount,” also falls in the realm of speculation of human conduct.

30. As regards the sum of Rs.40,95,724/- with the same understanding between the parties on which Dev Singh Palak has sent ₹60,000 to the assessee he must have sent the balance amount of Rs.40,95,724/-. If Dev Singh Palak has come forward to claim that the money belongs to him with proof, it is not within the power or jurisdiction of the AO to reject the same, more so when the lender's identity and capacity to lend are established. The AO has also assigned jejune reasons to reject

the documents filed by the assessee in support of the transactions. The AO addressed letter dt.29.12.2009 to the Director, FT and TR 1, New Delhi, wherein he has called for a detailed report on the transfer of funds from UK. The letter reads as follows:

“F. No.DCIT/CC-2/Hyd/S & S/2009-10

Office of the  
Deputy Commissioner of  
Income Tax,  
Central Circle-2,  
Aayakar Bhavan,  
Hyderabad.

29-12-2009

To  
The Director,  
FT and TR 1,  
Room No.908  
HUDCO Vishala building  
Bikajikama place  
New Delhi 110066

Sir,

Sub: Search and seizure assessment in the case of Sri P. Chandra Sekhar – AY 2005-06 to 2008-09. Huge amounts of NRI funds credited into the bank account of the assessee as loan and gift – Verification of identity and creditworthiness of the donor – regarding:

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Please refer to the above.

During the course of search assessment proceedings of the above said case it is noticed that the assessee was in receipt of loans and gifts from the following persons and credited the same into his bank account (A/c.No.737010054632 of ING Vysya Bank, Banjara Hills, Road No.2, Hyderabad). The details are furnished in the proforma enclosed. It is pertinent to mention here that the assessee has never filed any return of income till date of search i.e., 09.10.2007. After issue of notice u/s. 153A of the IT Act he has filed his return of income and disclosed the amounts mentioned in the proforma. As the funds are transferred from Birmingham, U.K. the reference has been made to FTD as per the

prescribed proforma. The information sought in the proforma may be investigated and a detailed report may be forwarded to the undersigned.

Yours faithfully,

(Dr. S. Palanikumar)  
Deputy Commissioner of Income Tax  
Central Circle-2, Hyderabad”

Proforma for seeking specific information under the provisions of “exchange of information”, article of double taxation avoidance agreement, was also enclosed to the said letter. In Sl. No.5, a sum of Rs.87,95,724/- was mentioned as the amount lent by Dev Singh Palak as loan to the assessee. Having thus sought for confirmation about the genuineness or otherwise of the transactions, from the Director, FT and TR 1, New Delhi, the AO was silent in his order as to whether he has received a report and, if so, to what effect. As rightly argued by the learned counsel for the assessee, failure of the AO to refer to his queries to the Director and the result thereof in his order would give rise to an adverse inference against the Revenue and in favour of the assessee that the report is favourable to him and that therefore the AO deliberately refrained from referring to the report.

31. The reliance of the AO on the pattern of the signature to arrive at the conclusion that Mr. Dev Singh Palak was not a man of means, reflects his highly archaic and imbalanced

approach. Such a test can never be applied to determine one's possession of means. The overwhelming material filed by the assessee explaining the cash receipt under item No.(ii) which remained unimpeached, renders the decision to treat the sum of Rs.87,95,724/- as unexplained credit, is wholly unjust and illegal. All the findings in support of such inclusion rendered by the AO and confirmed by both the appellate fora suffer from perversity.

32. Item No.(iii) relates to treating a sum of Rs.10,00,000/- claimed to be a loan from one J.V. Sudhakar as unexplained cash credit under Section 68 of the Act. The assessee's case is that during the financial year 2005-06, i.e., on 21.03.2006 he has received Rs.10,00,000/- as loan from one J.V. Sudhakar and that the same was repaid by him on 5.6.2006 by bank transfer. That as Mr. J.V. Sudhakar was not available during the assessment proceedings, he could not appear before the AO. However, the AO obtained bank statement from the bank concerned and that though the said bank statement has proved the bank transaction, the AO has added the same as unexplained cash credit under Section 68 of the Act and the said order was confirmed by the CIT (A) as well as the Tribunal.

33. To substantiate the plea of the loan, the assessee has filed the confirmation letter issued by J.V. Sudhakar wherein he has stated that he has given an unsecured loan of Rs.10,00,000 to the assessee by way of transfer from his bank account No.737010035602 with ING Vysya Bank Ltd. Banjara Hills, Hyderabad, on 21.03.2006 and that the loan amount was returned by the assessee on 25.07.2006 by transfer from the latter's account with ING Vysya Bank, Banrara Hills, Hyderabad.

34. The AO has observed that though the assessee has stated at page No.13 of the written submissions that the confirmation letter of J.V. Sudhakar was filed in annexure 16, a verification of the same shows that it is nothing but the assessee's bank account copy. Therefore, we are inclined to eschew the same for consideration.

35. It is evident from the AO's order that he has summoned the bank account statements pertaining to J.V. Sudhakar's account. While he did not doubt the correctness of the entries in the bank statement, the AO, however, relied upon the circumstances that the summons issued to J.V. Sudhakar were returned unserved with the endorsement that 'no such addressee was residing in that address'. From this fact, the AO

has concluded that the assessee has failed to establish the identity and creditworthiness of the lender and genuineness of the transaction.

36. A copy of the bank account statement of Mr. J.V. Sudhakar stated to have been obtained by the AO and filed in the appeal shows that on 21.3.2006 a sum of Rs.10,00,000/- was withdrawn from his account and transferred to the assessee's account, and on 25.07.2006 a sum of Rs.10,00,000/- was credited to the account of J.V. Sudhakar, transferred from account No.737010054632 which admittedly belongs to the assessee. This statement also shows that the bank account of J.V. Sudhakar was full of day to day transactions, and withdrawals and deposits of amounts upto around Rs.50,00,000/- were also shown on many occasions. The assessee also produced his own bank statement for the period 1.2.2006 to 31.3.2007 which shows that on 21.3.2006 a sum of Rs.10,00,000/- was credited to his account from the account of J.V. Sudhakar by way of transfer. The facts discussed above would not only show the genuineness of the transaction, but also the creditworthiness of the lender.

37. As regards the identity, the assessee is not a privy to the alleged return of the summons with the endorsement that no

such person is residing in the address. The identity of J.V. Sudhakar is clearly established from the bank account sent by ING Vysya bank, the authenticity and genuineness of which were not doubted by the AO. If the AO has entertained a doubt about the existence or otherwise of J.V. Sudhakar, in all fairness, he ought to have issued a notice to the assessee to produce the said Sudhakar, but he did not do so. Despite the availability of overwhelming and unimpeachable documentary evidence, the AO was not prepared to accept the same, as his approach appeared to be loaded with prejudice, suspicion and pre-determined mind and preconceived notions. The whole approach of the AO appears to be some how reject the every explanation of the assessee and the evidence produced in support of such explanation, by assigning reasons which are wholly imaginary and perverse.

38. As regards item No.(iv), the case of the assessee is that he has advanced a loan to a company by name M/s. Dakshin Shelters Pvt. Ltd., on various dates. That the company though credited interest in its books of account and deducted tax, has never paid the interest on the loan to the assessee, that the assessee followed cash system of accounting and admitted the tax deducted at source as income and claimed the credit for

TDS. That during the course of assessment proceedings, the assessee submitted that the interest income in its entirety was not admitted. That the AO, ignoring the provisions of Section 145 of the Act, which mandates admission of income on the basis of accounting method, erroneously relied upon Section 5 of the Act for treating the interest income as taxable. While confirming the order of the AO, the Tribunal held that once the assessee claimed credit towards TDS on the interest income, it cannot be said that for the other portion of interest the assessee is following cash system of accounting, that claiming of credit towards TDS and claiming of deduction of interest income shall go together and that therefore there cannot be dual method for the same income.

39. The learned counsel for the assessee submitted that as the company was following the mercantile system of accounting, it has deducted TDS on the assumption of payment, though it was not actually paid and that when it comes to the assessee, who was following the cash system of accounting, he has not admitted the same as income as the company has not paid the same. The learned counsel relied upon the clarification issued by the CBDT on the recently introduced provisions of Income Computation and Disclosure Standards. He has also submitted

that the view taken by the Tribunal relying upon the assessment on the basis of claim for TDS is contrary to the provisions of Section 199 of the Act, which envisages that the credit shall be given in the year when the income is assessable. That the assessee has admitted income to the extent of TDS on receipt basis/cash basis and that once this income is admitted there is no error in claiming credit for TDS. He has further submitted that the AO could have at best directed to restrict the claim of TDS in proportion to the income admitted and allowed the balance in the year in which the interest income is admitted on receipt basis. The learned counsel further submitted that the assessee has admitted the entire interest income for the year 2012-13 as in the previous year relevant to that assessment year, and the deposit was converted into shares by M/s. Dakshin Shelters Pvt. Ltd. In the grounds appeal, a detailed explanation has been offered by the assessee, which reads as under:

“...The treatment of the TDS amount and the non-received receipt balance interest operate in two distinct spheres and have no linkage with each other. The income tax authorities takes away the TDS which is served to it on a platter. It cannot have the cake and eat it too. It cannot dictate terms to the Appellant/Assessee who is mandated to follow one of the two accounting methods under Section 145 of the IT Act. He also cannot have two modes of accounting at the same time for the same Assessee.

Adding the unreceived income to the income of the Appellant/Assessee when he has not received it can have alarming and disastrous consequences. In the event of the loanee company going into liquidation, the Appellant/Assessee may not

get back his interest or principal. Being unable to meet its liability to its creditor, the loanee company chose to issue equity shares to its creditors. So, whereupon, the interest loan and interest liability to the loanee company stood extinguished. Having not received the interest income year after year and with no reasonable prospect of receiving it ever as subsequent developments have shown, and coercing the Appellant/Assessee to account for it as income for the year and on top of it, pay tax for the same, is unreasonable, unjust and iniquitous. Such an interpretation of the Income Tax Act would not have been envisaged by the legislators. In equity and good conscience, the income tax, surcharge, penalty, etc., imposed on the non-received income is liable to be recalled and the TDS credit received should remain in the credit of the Appellant/Assessee to be adjusted against past or future income tax liability.

The Assessing Officer made an incorrect addition of Rs.3,05,753/- under the head interest income by holding that even though the Appellant/Assessee had enclosed the TDS certificate, he did not include the balance of interest due to him, but not received by him, to tax, by disregarding the fact that the Appellant/Assessee was following the cash system of accounting.

The non-payment of interest of the loanee company to the Appellant/Assessee was due to the fact that it did not do any business except saving application money from applicants for allotment of equity shares and unsecured lenders which was utilised by the loanee company to buy peace from the landowners from whom land was taken for development. The loanee company could not go beyond this stage of business in view of prohibition orders of the Government, prohibiting development of land falling in the Bio-Conservation Zone. Following the impasse created by this prohibition, the loanee company which had blocked its finances for the land deal, suffered losses and had lost its capacity to repay its loans and meet its interest liabilities. On account of this, the loanee company capitalised the unsecured loans and unpaid interest in its hands due to Appellant/Assessee and capitalised it into equity share during the year 2011-2012 and issued equity share certificates in lieu of unsecured loans and unpaid interest thereon. The loanee company has adopted this uniform policy in case of all other lenders.

The Appellant/Assessee appealed against the assessment order inter alia contending that though the amount remained in the books of accounts in the loanee company as due to the Appellant/Assessee, the amount was not paid to him. Hence, the Appellant/Assessee who has been following the cash system of accounting consistently, had filed his return of income in the manner he did as the amount did not reach his hands ever. Unfortunately, the CIT(A) took an erroneous view of the facts and the law and upheld the additions made by the Assessing Officer, by giving a go-bye to the provisions of Section 145 which

permits an Appellant/Assessee to opt for one of the two approved accounting methods and not an amalgam of them.”

Section 145 of the Act reads as under:

**Method of accounting.**

**145. (1)** Income chargeable under the head “Profits and gains of business or profession” or “Income from other sources” shall, subject to the provisions of sub-section (2), be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee.

(2) The Central Government may notify in the Official Gazette from time to time income computation and disclosure standards to be followed by any class of assessee or in respect of any class of income.

(3) Where the Assessing Officer is not satisfied about the correctness or completeness of the accounts of the assessee, or where the method of accounting provided in sub-section (1) has not been regularly followed by the assessee, or income has not been computed in accordance with the standards notified under sub-section (2), the Assessing Officer may make an assessment in the manner provided in section 144.”

40. It is evident from the above extracted statutory provision that the assessee shall be free to follow either cash or mercantile system of accounting. Perhaps the only condition to be fulfilled by an assessee in this regard is whatever method he follows must be consistently followed without switching over from one method to the other frequently. It is not in dispute and cannot also be disputed that unlike mercantile system, in cash system of accounting return is filed based on actual receipt basis. The Government of India, Ministry of Finance, Department of Revenue, Central Board of Direct Taxes (TPL Division) vide Circular No.10/2017, dt.23.3.2017 has issued

clarifications to various questions. Question No.13 and the answer, which are relevant for the present purpose, read as under:

Question 13: The condition of reasonable certainty of ultimate collection is not laid down for taxation of interest, royalty and dividend. Whether the taxpayer is obliged to account for such income even when the collection thereof is uncertain?

Answer: As a principle, interest accrues on time basis and royalty accrues on the basis of contractual terms. Subsequent nonrecovery in either cases can be claimed as deduction in view of amendment to S.36(1)(vii). Further, the provision of the Act (e.g. Section 43D) shall prevail over the provisions of ICDS.”

41. In his order, the AO has proceeded on the assumption that since interest has accrued in the account books of M/s. Dakshin Shelters Private Limited, there is no prohibition on the assessee to withdraw the amounts from the unsecured loan amount in the books of M/s. Dakshin Shelters Private Limited. He has further observed that in the instant case, the assessee has received the interest income, but chose to keep it in the account in order to get interest on such income also.

42. As regards the first mentioned aspect, it defies any logic for, crediting of interest in account books does not enable the assessee to withdraw the amount as the same was not physically made available by M/s. Dakshin Shelters Private Limited for the assessee to make such withdrawal. The finding that the assessee has received interest income but chose to keep it in the

account in order to get interest, is in conflict with his previous observations that there is no prohibition for the assessee to withdraw the interest on the unsecured loan in the books of account of the company. Indeed, the Revenue has not disputed the claim of the assessee that the loanee company converted the unsecured loan and unpaid interest into equity shares during the year 2011-12 and accordingly issued equity shares certificates in lieu of repayment of unsecured loans and unpaid interest thereon. As submitted by the learned counsel for the assessee, the AO could have at best directed to restrict the claim of TDS in proportion to the income admitted and to allow the balance in the year in which interest income is admitted on receipt basis.

43. Item No.(v), which is the subject matter of I.T.T.A. No.720 of 2016, relates to inclusion of Rs.14,50,000/- allegedly received from Smt. P. Shanti Chowdhary, wife of the assessee, in the income as unexplained credit under Section 68 of the Act. The explanation offered by the assessee was that during the financial year 2005-2006 he received the aforementioned amount as loan from his wife by way of transfer from her bank account to his bank account on three dates. He has explained to the AO that the loan was given from out of gifts received by

his wife from her father in U.K. to whom the assessee's wife is the only daughter. The AO rejected the assessee's explanation and included the said amount as unexplained credit. The CIT(A), however, has reversed the order of the AO accepting the assessee's explanation. But, the Tribunal has upheld the order of the AO setting aside the order of the CIT(A).

44. In his order, the AO has referred to the confirmation letter dt.17.09.2009 issued by the assessee's wife stating therein that she has transferred Rs.3,00,000/-, Rs.3,90,000/- and Rs.7,50,000/- on 19.12.2005, 27.01.2006 and 31.03.2006 respectively to her husband as loan. That the assessee's wife has not appeared in response to summons dt.18.11.2009 and failed to furnish the books of account maintained by her for the financial years 2001-02 to 2007-08; the returns of income filed by her for the said period; the copies of bank account held by her individually as well as jointly for the said period maintained in India as well as in abroad; and the copy of her Passport. He has referred to the letter dt.25.11.2009 sent by the assessee stating that his wife is presently in Birmingham, U.K. and is expected to come back to India only in January, 2010. In her absence, the assessee gave the following information.

- (i) "She did not live in India during the F.Y. 2001-02 to 2005-06;

- (ii) Hence, she did not maintain any books of accounts and also not filed any return of income;
- (iii) She has not maintained any joint bank account in India or Abroad;
- (iv) As she went to abroad her copy of passport is not readily available.”

The AO commented that if the assessee’s wife was not in India, it is not known how confirmation letter dt.17.09.2009 could be filed before the AO on 20.10.2009. That her passport was not produced by the assessee in order to verify the entire claim and that she was not having any source of income nor did she file any return of income in India. The AO has expressed the following doubts which we find are rather unusual.

“If at all the assessee needs any money he can directly take from his father-in-law. It is not known why the money should be routed through the account of Smt. P. Shanti Chowdary and in turn should come into the bank account of the assessee. The assessee has invested these amounts only for the purpose of real-estate transactions. Under these circumstances, the identity and creditworthiness as well as genuineness of the transaction is not established by the assessee. Hence, the entire amount of Rs.14,50,000/- is added back to the total income of the assessee.”

45. The CIT(A) while reversing the order of the AO, gave the following reasons.

“I have considered the submissions as well as the facts of the case. There is no dispute about the identity of Smt. P. Shanti Chowdary, wife of the appellant. She has confirmed that she has lent the above sum of Rs.14,50,000/- to the assessee during the year. In fact the amount received from Smt. P. Shanti Chowdary during the year is Rs.14,40,000/- received on 3 different occasions of Rs.3 lakhs, Rs.3.90 lakhs and Rs.7.50 lakhs. The said amounts have been transferred from the bank a/c maintained at ING Vysya Bank, Banjara Hills, Hyderabad to the assessee who is also having bank a/c in the same branch. Even assuming that the gifts received by Smt. P. Shanti Chowdary from her father as bogus, still the loan received from her cannot be treated as unexplained

income of the assessee. Action can be initiated under Income-tax provisions to tax the so called gifts received by Smt. P. Shanti Chowdary in the respective years as unaccounted income. But as far as the assessee is concerned, the amounts have been transferred from the bank a/c of Smt. P. Shanthi Chowdary whose identity has been clearly established and confirmed by her, cannot be treated as unexplained income in his hands. Accordingly, the AO is directed to delete the addition of Rs.14.50 lakhs as computed by him and recomputed the total income. However, AO is directed to initiate appropriate proceedings under I.T. Law to bring the so called gifts received by Smt. P. Shanthi Chowdary to tax over the years.”

46. The Tribunal has reversed the order of the CIT(A) by advancing generic reasons, such as merely by filing confirmation from his wife, the assessee cannot make a non-genuine transaction as genuine and that in order to discharge the onus cast on the assessee under Section 68 of the Act, he has to establish not only identity of the creditors and confirmation of the credits, but also the capacity of the creditors to advance money as well as genuineness of the transactions.

47. Apart from the confirmation letter of his wife regarding transfer of amounts from her account to the assessee's account, the assessee has filed bank statements of his wife showing transfer of the amounts to the assessee's account. He has also filed copies of passport of his wife issued by United Kingdom of Great Britain and Northern Ireland and the residential permit dt.9.11.2006 issued by the Commissioner of Police,

Hyderabad City, showing that the assessee's wife is a U.K. nationality holding UK Passport and permitted her to remain in India until 02.02.2010. The assessee also produced certificate dt.26.3.2009 issued by the ING Vysya Bank to the effect that there was a Foreign Inward Remittance of GBP 400,000 to the credit of the assessee's wife on 16.05.2006 and the remittance was received from NatWest Bank from the account of Mr. Babu Rao Choudary Chaparala (the assessee's father-in-law) and the same was converted to FCNR deposit bearing No.123092135700 on 17.05.2006. The extract of the bank account of Dr. BC Chaparala with C&G Cheltenham & Gloucester is also filed to show that a sum of GBP 400,000 was transferred from the account of Babu Rao Choudary Chaparala to the account of P. Shanti Chowdary, wife of the assessee. Letter dt.17.9.2009 of Baburao C. Chaparala addressed to the AO confirming that he has given the said amount as gift to his daughter - P. Shanti Chowdary and that the said gift was made by him towards natural love and affection for her and the same has been accepted. He has further stated that he and his wife Dr. Bharathi Chowdary Chaparala are British Citizens and have been working in the United Kingdom for the National Health Service for over 30 years and that these amounts are out of

their joint savings and earnings. He has also enclosed a table giving the details of the amounts.

48. The material filed by the assessee shows that as in the case of the loan advanced by Mr. Dev Singh Palak, the AO has sought for specific information under the Provisions of “Exchange of Information” Article of Double Taxation Avoidance Agreement, to the Director, FT and TR1, Bikajikama place, New Delhi, to verify and report on the genuineness or otherwise of amount of Rs.1,52,00,000/- and Rs.1,30,00,000/- transferred by the assessee’s wife for the assessment years 2007-08 and 2008-09; amount of Rs.11,97,267/- and Rs.3,40,000/- transferred by Baburao Chowdary, to his daughter as gifts in the assessment years 2005-06 and 2006-07.

49. One cannot but be left wondering as to what better evidence one could have produced to establish the identity, genuineness and authenticity of the transaction of the loan. When the father-in-law of the assessee has himself given the confirmation letter that he has given the amount towards gift out of love and affection, we find no justification whatsoever for the AO and the Tribunal to raise doubt about the capacity of the assessee’s wife to lend the money. Both the parents of

the assessee's wife are not only British citizens, but also Doctors for over 30 years. Therefore, neither their capacity to gift the money nor their intention in doing so could be suspected. The evidence produced by the assessee is of such high standard that the approach of the AO in rejecting such evidence can only be termed as myopic. While the authorities are entitled to examine each transaction minutely, they cannot approach every transaction with undue suspicion by wearing coloured glasses. The approach of the AO reminds us of somebody describing a lamb as a dog and trying to make everyone to believe it to be so.

50. The learned counsel for the assessee was critical of the approach of the CIT(A) who while reversing the order of the AO directed him to initiate appropriate proceedings under the I.T. Law to bring the so called gifts received by the assessee's wife to tax over the years, on the ground that this direction was issued behind her back. However, we are not inclined to render any findings thereon. If any such proceedings are initiated by the AO, the assessee's wife shall be free to question the same on all sustainable legal grounds.

51. In our opinion, all the transactions, namely, gift of Rs.73,00,000/- made by the maternal aunt of the assessee; loan of Rs.87,95,724/- received from Dev Singh Palak; loan of Rs.10,00,000/- advanced by J.V. Sudhakar and repaid by the assessee and the loan of Rs.14,50,000/- received from the wife of the assessee are genuine and the onus cast on the assessee under Section 68 of the Act has been duly discharged with reference to the identity of his creditors, genuineness of the credits and also the capacity of the creditors to advance the money. The findings rendered by the AO and confirmed by the CIT(A) and the Tribunal, in cases other than the loan advanced by the assessee's wife, and that in respect of the said transaction the findings rendered by the AO and confirmed by the Tribunal, suffer from perversity. All the reframed substantial questions of law in both the appeals are accordingly answered in favour of the assessee and against the Revenue.

52. It is, however, directed that in respect of item No.(iv), the AO shall restrict the claim of TDS in proportion to the income admitted for the assessment year 2005-06 and allow the balance in the year in which interest income is admitted on receipt basis.

53. The impugned orders of the Tribunal are accordingly set aside and both the appeals are allowed.

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C.V. NAGARJUNA REDDY, J

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CHALLA KODANDA RAM, J

23-2-2018

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Note: LR copies to be marked.

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