



TC (A) No. 1512 of 2008

IN THE HIGH COURT OF JUDICATURE AT MADRAS

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DATED : 19.01.2022

CORAM :

THE HONOURABLE MR. JUSTICE R. MAHADEVAN
and
THE HONOURABLE MR. JUSTICE MOHAMMED SHAFFIQ

Tax Case (Appeal) No. 1512 of 2008

M/s. Keld Ellentoft India Pvt Ltd.,
No.1-5, Vyasarpadi Industrial Estate
Vyasarpadi
Chennai - 600 039

.. Appellant

Versus

The Assistant Commissioner of Income Tax
Central Circle III (3)
108, Mahatma Gandhi Road
Chennai - 600 034

.. Respondent

Appeal filed under Section 260-A of The Income Tax Act, 1961 against the Order dated 02.05.2008 passed in I.T. (SS) A No.3/MDS/07 on the file of The Income Tax Appellate Tribunal, Chennai "B" Bench.

For Appellant : Mr. G. Baskar
for Mr. N. Muthukumar

For Respondent : Mr. Karthick Ranganathan, Sr. Standing Counsel
assisted by Mr. Rajesh, Junior Standing Counsel



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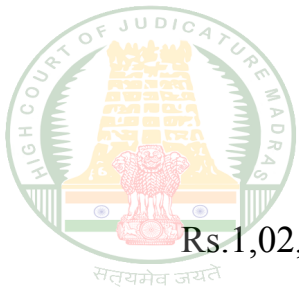
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JUDGMENT

R. Mahadevan, J.

This is an assessee's appeal against the order dated 02.05.2008 passed by the Income Tax Appellate Tribunal, Chennai "B" Bench in I.T. (SS) A No.3/MDS/07.

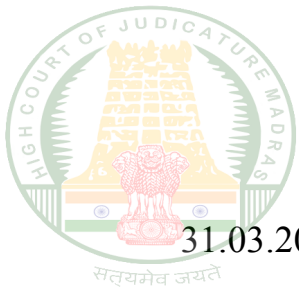
2. The assessee is a registered company engaged in the business of Non-Metallic Expansion Joints/Fabric Compensators/Flexible Connections. During the course of their business, search under section 132 of the Income Tax Act, 1961 along with a survey under section 133A were carried out simultaneously in the residential premises of the Managing Director of the assessee firm as well as in the place of business on 31.03.2003. Based on the incriminating materials recovered during the same, proceedings under Section 158BC read with Section 158BD of The Income Tax Act, 1961 (in short, 'the Act') were initiated by the respondent. Pursuant to the same, notice dated 19.03.2004 was issued calling upon the assessee firm to file their return of income for the block period between 1997-1998 to 2002-2003, upto 31.03.2003. Upon receipt of the same, by a reply dated 30.04.2004, the assessee sought extension of time to file their return, which was not acceded to. Finally, they filed their return on 20.12.2004 admitting a total income of



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Rs.1,02,00,000/- during the block period upto 31.03.2003. After examining the statement of the Managing Director of the assessee firm, the documents recovered during the search and also the return filed by the assessee firm on 20.12.2004, the respondent, by the assessment order dated 21.07.2005, determined the total and undisclosed income of the assessee firm at Rs.1,85,47,438/- and levied tax and surcharge thereon.

3. Aggrieved by the order of assessment passed by the Assessing Officer, the assessee firm filed an appeal before the Appellate Authority, wherein, it was contended on the side of the assessee that in para No.10.41 of the assessment order, the Assessing Officer made a disallowance of Rs.72,32,972/- under Section 40A (3) of the Act stating that "*as the purported grey market purchases had been made in excess of Rs.20,000/- in cash in each and every single instance from unidentified sources, the provisions of Section 40A (3) are applicable to the case of the assessee*". Whereas, according to the appellant / assessee, the purchases made in the grey market were on *ad hoc* basis and no single purchase exceeded the limit of Rs.20,000/- and therefore, invoking the provisions of Section 40A(3) is only on presumption. The appellant / assessee also contended before the Appellate Authority that the assessing officer treated the four items of outstanding credits as income as on



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31.03.2003 without application of mind to the provision of Section 41 (1) of the Act. Referring to Explanation I to Section 41 (1), which states that "*loss of expenditure or some benefit in respect of any such trading liability by way of remission or cessation thereof shall include the remission or cessation of any liability by a unilateral act by the first mentioned person under clause (a) or the successor in business under clause (b) of that sub-section by way of writing off such liability in his accounts*", it was contended that the outstanding credits can be treated as income by the Assessing Officer only based on the entries in the books of accounts made by the appellant / assessee and hence, the same cannot be the subject matter of addition in the block assessment.

4. The appellate authority, on examining the order of assessment passed by the assessing officer as well as the grounds raised by the appellant, partly allowed the appeal as indicated below:-

4.3

it is clear that in a case where net profit has been determined on the basis of estimation, further disallowance u/s. 40A(3) is invalid. In view of the facts of the case and in law, it is held that disallowance of Rs.72,32,972/- u/s.40A(3) and assessing it as undisclosed income for the block period is invalid, hence, the same is deleted. This ground of appeal is allowed.

5.3 I had examined the facts of the matter and studied the provisions of law and case laws relating to the issue. The

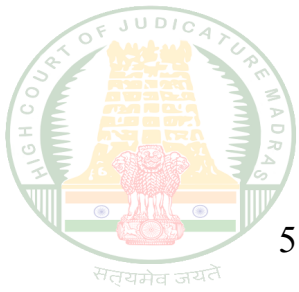


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AO's finding that the facts and circumstances of the case suggest that cessation has occurred is plausible. However, his judgment to ignore the fact that the two trade liabilities in respect of S&S Engineers & Contracts and M/s. Sri Amman Trading Co., have been written off in the regular books of accounts for financial year 2002-2003 and the same is offered to tax in the return of income for financial year 2003-04 is not genuine....

5.4 The provision of liability clearly shows that it is for the assessee to decide as to when the cessation of liability occurred and in which previous year he has to write it off. In the appellant's case the two trade liabilities were treated by the assessee to have cessation and that the cessation of liability has occurred in the financial year 2002-2003. There is no reason to dispute the assessee's judgment that cessation of liability in respect of two concerns had occurred in the financial year 02-03. Since the two liabilities have been written off in the year 02-03 and has been offered to tax under Section 41 (1) in the return of income u/s.139 there is no justification for treating these two trade liabilities as undisclosed income. Nevertheless in respect of the other two trade liabilities totalling to Rs.1,56,776/- it is reasonable to hold that cessation has occurred but the same has not been written off in the books of accounts. The addition in respect of these two trade liabilities is justified. In view of the above discussion the addition of Rs.11,14,466/- is reduced to Rs.1,56,776/-. This ground of appeal is partly allowed.

5.5 In Ground No.4, levy of interest at Rs.10,51,640/- u/s.158BFA is challenged. On examination of the facts and provisions of law, it is found that the interest u/s.158BFA is chargeable in case of the assessee. However, the AO is directed to re-compute the interest u/s.158BFA at the time of passing the appeal effect order."



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5. Aggrieved by the order passed by the Appellate Authority, the

Revenue preferred an appeal before the Tribunal and the appellant also filed cross objection. The Tribunal accepted the plea of the Assessing Officer and reversed the order passed by the appellate authority with the following observations:

"3.5 Upon a careful consideration we find that it is not at all the Assessing Officer's case that these sums are being taxed u/s.41 (1). When certain trade liabilities of the assessee incurred in the normal course of trade are no longer payable, the same is liable to be included in the income of the assessee and the amount as such is taxable. For this proposition, we rely upon the decision of the Honourable Apex Court in the case of CIT vs. T.V. Sundaram Iyengar and Sons Limited, 222 ITR 344 (SC).....

On the anvil of aforesaid decision, these sums which were trade liabilities no longer payable are very much assessable in the hands of the assessee. Further the fact that two of the sums were offered for taxation in the return filed for financial year 2002-2003 after the date of search, cannot be a basis for deletion of these additions for block assessment. Hence, we set aside the order of the learned Commissioner of Income Tax (Appeals) and restore that of the Assessing Officer."

6. As against the order passed by the Tribunal, setting aside the order of the Appellate Authority and restoring the order of the Assessing Officer with respect to addition of Rs.11,14,466/-, the assessee is before this Court with this tax case appeal.



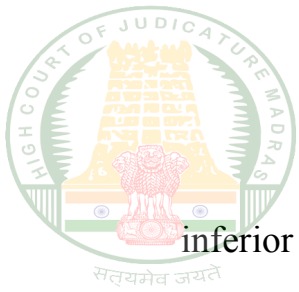
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WEB COPY 7. At the time of admission of this appeal on 20.10.2008, the following substantial question of law was framed for consideration:-

"Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal is right in law in holding that the amount of Rs.11,14,466/- represented "undisclosed income" of the assessee for the purpose of Chapter XIV B of the Income Tax Act?

8. The learned counsel for the appellant submits that the assessing officer completed the assessment proceedings by determining the total and undisclosed income of the assessee at Rs.1,85,47,438/-. Out of the amount determined by the assessing officer, the appellant / assessee is aggrieved by the addition made towards certain outstanding credits over a period of time amounting to Rs.11,14,465/- payable to the dealers namely (i) M/s. S&S Engineers and Contracts to the tune of Rs.8,27,914/- (ii) M/s. Sriram Sales & Suppliers for Rs.1,33,716/- (iii) M/s. Sri Amman Trading Company for Rs.1,29,776/- and (iv) Modern Packers for Rs.23,060/-, which amounts were treated as income under Section 41(1) of the Act. The assessing officer concluded so, based on the entries reflected in the books of accounts maintained by the appellant / assessee. According to the learned counsel, the said amounts were withheld due to poor performance of the contractor and/or

there was a dispute between the said traders and the appellant as regards the



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inferior quality of supplies effected. Furthermore, the appellant has been continuing the business transaction with the said dealers; and the sum of Rs.8,27,914/- was offered to tax by the appellant in the return filed for the year 2003-2004. With regard to the remaining entities, on account of the on-going business relationship, they were not reversed in the books of accounts. In any event, the outstanding credits had not been claimed as deduction in any previous years. While so, the Tribunal erred in holding that the sum of Rs.11,14,465/- has to be treated as undisclosed income and the same is liable to tax. The learned counsel further submits that these amounts indicated in the books of accounts as outstanding credits and there was no other material recovered during the search to conclude that the same were undisclosed income under Chapter XIVB. Whenever addition is sought to be made as "undisclosed income", it must be supported by material evidence seized during the search or it should emanate from the materials gathered during the search. In the absence of any material seized during the search to substantiate the addition, it cannot be legally sustainable. Further, the Assessing Officer, on assumption, concluded that the cessation of liability had occurred and therefore, the amounts have to be treated as undisclosed income, but he failed to note that cessation of tax liability is a subject matter of Section 41 (1) of the Act, which does not get attracted to the facts of the present case. An amount

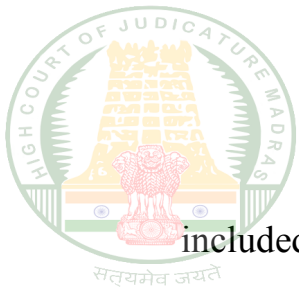


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would be chargeable as an assessee's profit only whether an allowance or a deduction is made in respect of such amount in the previous year. Whereas, in the present case, the amounts have been withheld by the assessee due to non-performance of the obligations under the contract or there was inferior quality of the materials supplied to the assessee. In such circumstances, it cannot be said that the appellant / assessee has gained profit out of such amounts warranting addition by treating it as 'undisclosed income'. Stating so, the learned counsel sought to allow this appeal by setting aside the order passed by the Tribunal.

9. On the other hand, the learned senior standing counsel appearing for the respondent submits that only after the conduct of search, the assessee filed their returns and that, though two of the amounts were offered for taxation in the return filed by them, the same were not already written off in their books of accounts maintained upto 31.03.2003. Therefore, the assessing officer, on careful examination of the materials placed, came to the conclusion that the static credit balances shown as liabilities outstanding are no longer held so, in the absence of any confirmatory letters from the said parties. According to the learned counsel, when a particular amount payable to a party during the course of business is not paid and withheld, the same has to be



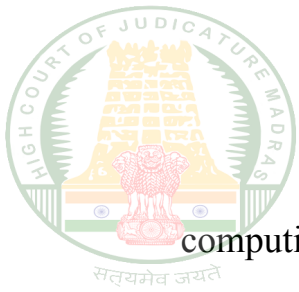
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included in the income of the assessee and is taxable. In this context, the learned counsel relied on the decisions of this Court in **R.Rangasamy v. Deputy Commissioner of Income Tax, Central Circle III [264 CTR 410 (Madras)]** and the Patna High Court in **Commissioner of Income Tax, Central, Patna vs. Harsh Kochar [(2016) 69 Taxmann.com 322 (Patna)]** and submitted that if, based on the materials seized during search, additions are made by the Assessing Officer, such determination cannot be said to be arbitrary and hence, the Tribunal has rightly held that when certain trade liabilities of the assessee incurred in the normal course of business are no longer payable, the same are liable to be included for tax treating it as undisclosed income. Thus, the learned counsel prayed for dismissal of the appeal filed by the assessee.

10. We have heard the counsel for both sides and perused the materials placed before us.

11. Concededly, pursuant to the search as well as survey and initiation of the proceedings under section 158BC read with section 158BD, the appellant filed their return for the block period, admitting the total income at Rs.1,02,00,000/-. The assessing officer, after completing the assessment,



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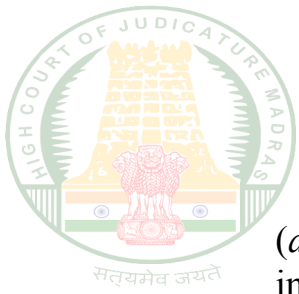
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computing the total and undisclosed income at Rs.1,85,47,438/- and raising a total demand of Rs.62,07,740/-, after deducting the tax already paid by the assessee. The assessee went on appeal before the appellate authority, to whom, two main issues were raised viz., (i) disallowance under section 40A(3) to the tune of Rs.72,32,972/- and (ii) certain outstanding credits amounting to Rs.11,14,465/- were treated as income under section 41(1) of the Income Tax Act, 1961. There is no dispute that the first issue was decided in favour of the assessee by the appellate authority and the same was also confirmed by the Tribunal. Regarding the second issue, the appellate authority partly allowed the claim of the assessee by reducing the addition from Rs.11,14,465/- to Rs.1,56,776/-. However, the Tribunal set aside the said order of the appellate authority and restored the order of the assessing officer, by order dated 02.05.2008, which is impugned in this tax case appeal.

12. Before proceeding further, it would be relevant to extract the relevant provision of law involved herein, viz., section 41(1) of the Act, which reads as follows:

“Profits chargeable to tax.

41.(1) Where an allowance or deduction has been made in the assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee (hereinafter referred to as the first-mentioned person) and subsequently during any previous year,—



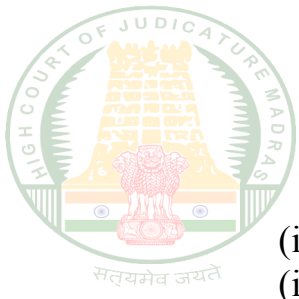
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(a) the first-mentioned person has obtained, whether in cash or in any other manner whatsoever, any amount in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cessation thereof, the amount obtained by such person or the value of benefit accruing to him shall be deemed to be profits and gains of business or profession and accordingly chargeable to income-tax as the income of that previous year, whether the business or profession in respect of which the allowance or deduction has been made is in existence in that year or not; or

(b) the successor in business has obtained, whether in cash or in any other manner whatsoever, any amount in respect of which loss or expenditure was incurred by the first-mentioned person or some benefit in respect of the trading liability referred to in clause (a) by way of remission or cessation thereof, the amount obtained by the successor in business or the value of benefit accruing to the successor in business shall be deemed to be profits and gains of the business or profession, and accordingly chargeable to income-tax as the income of that previous year.

Explanation 1.—For the purposes of this sub-section, the expression "loss or expenditure or some benefit in respect of any such trading liability by way of remission or cessation thereof" shall include the remission or cessation of any liability by a unilateral act by the first-mentioned person under clause (a) or the successor in business under clause (b) of that sub-section by way of writing off such liability in his accounts."

13. According to the order of assessment, based on the books of accounts of the appellant / assessee, wherein, it was found that certain credits were shown as outstanding over a substantial period of time and the same were no longer payable by the assessee company, the assessing officer made those credits of Rs.11,14,465/- as addition treating it as undisclosed income, the details of which are reproduced below:



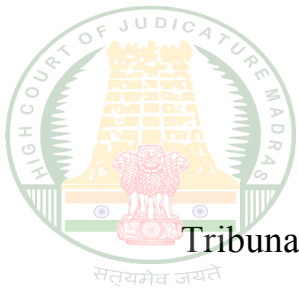
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(i)S&S Engineers & Contracts -	Rs. 8,27,914/-
(ii)Sriram Sales & Suppliers -	Rs. 1,33,716/-
(iii)Sri Amman Trading Co -	Rs. 1,29,776/-
(iv)Modern Packers -	Rs. 23,060/-

14. It is the stand of the appellant / assessee that they were continuing business transactions with the aforesaid four companies and withholding certain amounts payable to them, due to incomplete work / dispute as regards the quality of materials supplied. However, with respect to the amount of Rs.8,27,914/-, the same was offered to tax in the return filed for the assessment year 2003-04. In respect of other three entities, on account of the on-going business relationship, the outstanding credits had not been reversed by the appellant. However, the same had not been claimed as deduction in any previous year. On consideration of the same, the appellate authority held that the amounts payable to M/s.SS Engineers & Contractors and M/s.Sri Amman Trading Co. were written off in the regular books of accounts only in the year 2002-03 and accordingly, offered to tax in the year 2003-04, the disallowance on those amounts would have to be cancelled; and it is for the assessee to decide as to when the liability ceased, which is relevant and whether the amounts have actually accrued as income; and the appellant did not apply the said logic with respect to two other liabilities amounting to Rs.1,56,776/- and

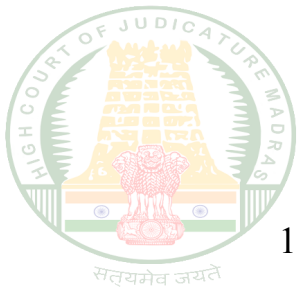
hence, the addition of Rs.11,14,466/- was reduced to Rs.1,56,776/-. But the



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Tribunal erred in setting aside the said order of the appellate authority and confirmed the order of the assessing officer, on the premise that the appellant's return offering two out of the four credits for tax, was filed only after the search proceedings. It is the further case of the appellant that the assessing officer on the assumption, rendered a finding that cessation of the liability had occurred, as per which, the amounts were taxable under section 41(1) of the Act, as undisclosed income and hence, the said provision is not applicable to the facts of the present case.

15. We find that the Tribunal after careful analysis of the materials, has held that only after the search, the assessee came forward and offered two of the four amounts for taxation as liability no longer in existence in the return filed for the financial year 2002-03; and that, it was not the case of the assessee that these sums were already written off in the books upto 31.03.2003. Further, it was pointed out by the Tribunal that the assessing officer made the additions by holding that the static credit balances shown as liabilities outstanding are no longer held so, in the absence of any confirmatory letters from the said parties and hence, the same are forming part of the undisclosed income of the block period. After holding so, the Tribunal rejected the contention of the assessee and set aside the order of the appellate authority and thereby restored the order of the assessing officer.



16. In **R.Rangasamy case**, mentioned above, on the side of the Revenue, it was held by this court that the filing of returns by the assessee after the date of search and before issuance of notice under Section 158 BD of the Act would not in any manner make the return of income as valid and in such case, undisclosed income determined by the Assessing Officer cannot be said to be illegal. Paragraphs 10 and 11 of the said decision can be profitably extracted below:

"10. We disagree with the contention of the assessee. For a case of non-filing of return would be one where the due date for filing a return of income has expired, but no return of income has been filed by the assessee. Section 158 BB of the Act states that in such case the undisclosed income has to be computed as given under (c) (A), (c) (B) and (c) (ca). Thus, the computation of undisclosed income of the block period shall be the aggregate of the income could be determined on the basis of the entries as recorded in the books of accounts. The computation of the undisclosed income of the block period shall be the aggregate of the total income of the previous years falling within the block period, computed in accordance with the provisions of the Act. Thus, as far as clause (ca) is concerned, when the due date for filing of the return of income has expired and the assessee had not filed the return even as stating that it was 'nil' income, then Section 158BD would be of relevance.

11. Thus, having regard to the facts and the provisions of law narrated above, the case of the assessee would certainly fall for consideration under Section 158 BB read with 158 BD of the Act and the assessment could not be faulted with".

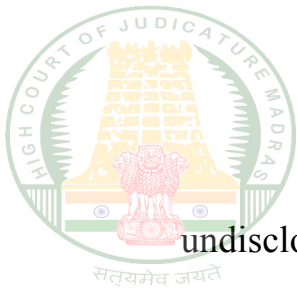


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WEB COPY17. In similar circumstances, the Patna High Court in **Harsh Kochar** case (supra), decided the appeal in favour of the Revenue, with the following observation:

“15. There is no dispute that there cannot be any estoppel against the statute, but once a provision is made for the benefit of an individual, such benefit can always be waived as there is no public interest involved in waiving such right. Even if, the documents were recovered from the premises of Sujata Hotel Pvt. Ltd but the assessee having filed his return on the basis of such documents, he cannot turn around to say that such documents cannot be referred to by the Assessing officer while framing assessment for the block assessment.”

18. Applying the aforesaid legal proposition to the facts of the present case, wherein, admittedly, the assessee filed their return only after the conduct of search. Based on the same, the assessing officer computed the total and undisclosed income and made additions to the tune of Rs.11,14,465/- for the block period. In such circumstances, the assessee ought to have rebutted the same by giving cogent and reliable evidence, whereas they failed to do so. Therefore, they cannot be permitted to contend that based on the books of accounts furnished by them, the assessing officer made such additions. Further, the liabilities were shown in the books of accounts as outstanding credits and the same were not written back by the assessee and hence, the Tribunal rightly justified the additions made by the assessing officer as



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undisclosed income under section 41(1) of the Act, which could not be faulted

with, in the opinion of this court. At this juncture, it is apt to refer to the

decision of the Hon'ble Supreme Court in the case of **Assistant Commissioner**

of Income tax, chennai v. A.R.Enterprises [2013] 29 taxmann. Com 50

(SC), in which, it was held as under:

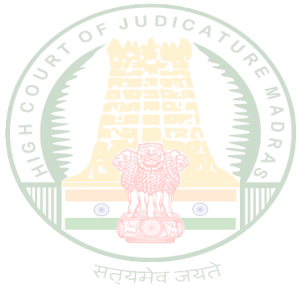
“39.Thus, for the purposes of computation of undisclosed income under Chapter XIVB, an assessee can rebut the Assessing Officer's finding of undisclosed income by showing that such income was disclosed in the return of income filed by him before the commencement of search or the requisition. In other words, when section 158BB(3) is read with section 158B(b), which defines undisclosed income, we reach the conclusion that for income to be considered as disclosed income, the same should have been disclosed in the return filed by the assessee before the search or requisition.”

19. Thus, for the discussions held above, we are of the opinion that there is no question of law much less substantial question of law raised in favour of the assessee. Accordingly, the tax case appeal deserves to be dismissed and is dismissed. No costs.

(R.M.D., J.) (M.S.Q., J.)

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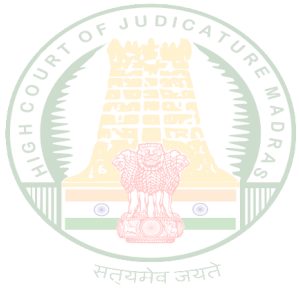
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- To
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Chennai - 600 034
 - 2.The Income Tax Appellate Tribunal, Chennai "B" Bench.



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R. MAHADEVAN, J
and
MOHAMMED SHAFFIQ, J

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