* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Reserved on: 1st April, 2014
% *Date of Decision: 15th April, 2014*

\+ ITA 244/2013

COMMISSIONER OF INCOME TAX DELH-II ..... Appellant
Through: Mr. Sanjeev Sabharwal, Sr. Standing Counsel with Sh. Ruchir Bhatia, Jr. Standing Counsel

versus

KALINDI RAIL NIRMAN ENGG. LTD. ..... Respondent
Through: Sh. R.K. Sharma, Advocate.

CORAM:
MR. JUSTICE S. RAVINDRA BHAT
MR. JUSTICE R.V. EASWAR

R.V. EASWAR, J.

1. This appeal filed by the revenue under Section 260A of the Income Tax Act, 1961 (hereinafter referred as the "Act") is directed against the order passed by the Income Tax Appellate Tribunal ("Tribunal", for short) on 29.03.2012 in ITA No.322/Del/2008 confirming the order of the Commissioner of Income Tax (Appeals) dated 26.10.2007 by which he cancelled the penalty of Rs.24,00,977/- imposed on the assessee under Section 271(1)(c) of the Act for concealment of income.

2. The assessee, a contractor undertaking projects of Indian Railways on turn key basis, filed its return of income for the assessment year 1995-96 on 29.11.1995 declaring a total income of Rs.88,91,700/-. On the basis of the materials gathered by the income tax authorities in the course of a search carried out in the assessee's premises on 14.03.1995 as well as in the premises of the directors and trusted persons, the assessing officer referred the matter to a special audit in terms of Section 142(2A) of the Act. The special audit report, *inter alia*, reported that there were large number of transactions for which no supporting vouchers were available, that several discrepancies in cash and journal vouchers and changes in the dates of the vouchers were noticed, that there were discrepancies in the adjustments of cash books with cash vouchers, that there were payments made to the Railway staff which were not allowable as deduction under the Act, that several payments were made without obtaining any signature of the recipients, that the assessee did not maintain any stock register and did not disclose any work-in-progress in the balance sheet, that several items of capital expenditure were passed off as revenue expenditure and so on and so forth. In response to the queries raised by the assessing officer on the basis of special audit report the assessee could not give any proper explanation and wherever an explanation was sought to be given, it was found to be evasive. The assessee was also allowed inspection of

the seized documents and was supplied photocopies of the seized records. Despite such opportunity, no convincing reason was given by the assessee to the query of the assessing officer as to why the results declared by the books of accounts could not be rejected and the profit from the contracts be not estimated at a rate exceeding 11% of the gross receipts. Not convinced by the assessee's explanation to the show-cause notice, which was only that the accounts maintained by the assessee were based on accounting policies consistently adhered to, the assessing officer proceeded to estimate the net profit of the assessee at 11% of the gross receipts from the contracts amounting to Rs.20,30,74,024/-, which came to Rs.2,23,38,143/-. The assessing officer also found that some income from business activities was not included in the aforesaid receipts and the profit from such activity was taken at Rs.13,34,308/-. The total business income was thus taken at Rs.2,36,72,451/- before allowing depreciation. Demands were accordingly raised.

3. It would appear that the assessee carried the matter in appeal to the Tribunal which by order dated 05.09.2002 passed in ITA No.28/JP/2000, reduced the income by adopting the profit rate of 8% on the gross receipts subject to allowance of depreciation and interest. The separate addition of Rs.13,34,308/- was deleted.

4. Penalty proceedings were initiated by the assessing officer for concealment of income and after rejecting the assessee's explanation, a minimum penalty of Rs.24,00,977/- was imposed for concealment of income under Section 271(1)(c) of the Act. The assessing officer held, overruling the assessee's explanation that merely because the profits were estimated, it does not follow that the assessee was not guilty of any fraud or gross or wilful neglect on his part to return the correct income, as provided in the Explanation below Section 271(1)(c) of the Act, as it stood at the material period.

5. The penalty order was taken in appeal to the CIT (Appeals) who cancelled the same on the ground that the assessing officer has not stated the basis of this estimate nor did he give an opportunity to the assessee to rebut the proposal to estimate the profits at 11% of the gross receipts. He held that the assessee made a counter proposal which was a conditional offer as to the taxability of the profits and even if it is assumed that there was an agreement on the part of the assessee for being taxed at the rate of 11% of the gross receipts, it does not follow automatically that the assessee concealed its income. The revenue's appeal to the Tribunal having been dismissed, it is in further appeal before this Court.

6. In our opinion the following questions of law arise for consideration: -

> *(i) Whether on the facts and in the circumstances of the case the Tribunal was right in law in upholding the order of the CIT (Appeals) cancelling the penalty imposed on the assessee for concealment of income under Section 271(1)(c) of the Act?*
>
> *(ii) Whether the view of the Tribunal that the assessee's acceptance of the profit rate of 11% was only a conditional proposal and made with a view to buy peace and avoid disputes, is a reasonable view or is it perverse?*

7. We have considered the rival contentions. While the revenue assails the order of the Tribunal on the ground that after the judgment of the Supreme Court in the case of *MAK Ltd. Data P. Ltd. vs. CIT*, (2013) 358 ITR 593 there is no question of the assessee offering income "to buy peace" and that in any case the seized material and the special audit report disclose several discrepancies to cover which a higher estimate of the profits was resorted to, the learned counsel for the assessee vehemently contended that the Tribunal committed no error in upholding the order passed by the CIT (Appeals) cancelling the penalty. He would contend that it was a mere case of different estimates of income being adopted by different authorities which itself would show that there is no merit in the charge of concealment of income. He further contended that the revenue is wrong in saying that a higher rate of profit was adopted to

cover the discrepancies pointed out in the special audit report, since there was nothing preventing the assessing officer from making separate additions if those discrepancies were not explained by the assessee as alleged by him. He filed a copy of the order of the Tribunal dated 05.09.2002 passed in the quantum proceedings to support his contentions. He also emphasised that the assessee had agreed to be assessed on 11% of the gross receipts only on the condition that no inference of concealment of income would be drawn from such concession and in such circumstances, where the offer was conditional and to buy peace, there can be no levy of penalty for alleged concealment of income.

8. The learned counsel for the assessee would have been right if it was a simple case of one estimate against another. However, where incriminating materials are gathered in the course of search conducted by the tax authorities and the special audit report, which is based on those materials, reports a number of discrepancies and irregularities in the maintenance of books of accounts, the case ceases to be a simple case of estimate of income and it is open to the assessing officer to conclude that the assessee concealed its income, provided the alleged discrepancies and irregularities are not properly explained. In such a case it is open to the assessing officer even to make a flat rate assessment, pitching the

percentage at high figure to cover up the discrepancies noticed in the special audit report and revealed by the seized material, instead of making separate additions. This is what has happened in the present case. The search took place on 14.03.1995, towards the close of the relevant counting period. Despite the search, in the return filed on 29.11.1995, the assessee chose to declare its income at an estimated 3% of the contract receipts of Rs.20,30,74,024/-; no attempt was made in the course of the assessment proceedings to justify the said estimate. The assessing officer, armed with the seized material and the special audit report, did comply with the rules of natural justice and called upon the assessee to justify the income returned and explain the discrepancies and irregularities noticed by the special auditor. When the assessee was unable to do so, the assessing officer had no option but to make an estimate of the profits by adopting a percentage sufficient in his opinion to cover the discrepancies revealed by the special auditor and the seized material. In doing this, he committed no error; he also committed no error of law in concluding that there was gross or wilful neglect on the part of the assessee in failing to return the correct income. The burden to show the contrary was, according to the assessing officer, on the assessee which the assessee failed to discharge.

9. The learned counsel for the assessee is not right in his contention that whenever an assessment is made by applying a flat rate of profit to the declared turnover or receipts, which is higher than the rate adopted by the assessee in the return of income, there can be no inference that the assessee concealed his profits. There is no such absolute proposition and this has been brought out by the Madras High Court in *Bashu Sahib vs. CIT*, (1977) 108 ITR 736. There the assessee who was a bus operator filed a return in which he estimated the income at Rs.8,000/- per bus which was on the basis of the income determined by the Tribunal in his own case for an earlier assessment year. In the course of the assessment proceedings he denied having maintained books of accounts and also did not produce the trip sheets, invoices and correspondence with the regional transport authorities. The assessing officer, therefore, enhanced the income from each bus to Rs.19,245/-. Such estimated assessments were made for two assessment years and in the later assessment year the income was estimated at Rs.22,000/- per bus. Penalty proceedings were initiated for concealment of income. The Madras High Court held that the assessee did not produce the relevant evidence despite being called upon and there was a finding by the Tribunal that the assessee chose to withhold the books of accounts. The assessee knew that the method adopted by him did not disclose the real income. Though he was in a

position to know his real income, he deliberately estimated it at a lower amount. The High Court, therefore, held that the penalty proceedings were justified. Dealing with the argument that in cases of estimate of profits there can be no concealment, and rejecting the same, the High Court observed as under: -

> "*We are also unable to agree with the argument that in all cases where the taxing authorities estimated the income at a higher figure than what was estimated by an assessee, no penalty was leviable. Where the estimate of the assessee amounts to deliberate under-estimate, an inference of concealment of income could certainly be drawn. The facts in the present case clearly show that the assessee had deliberately under-estimated his income in the two years under appeal.*"

10. A Division Bench of this Court was seized with the question in *Qammar-ud-din & Sons vs. CIT*, (1981) 129 ITR 703, *Ranganathan, J.* (as he then was) held as follows: -

> "*The obligation of filing of a return is a solemn and important one and should not be undertaken in a lighthearted and careless manner. It may be that, in some circumstances, an assessee may have to estimate its income, but if so, such estimate should have some basis therefor. An assessee cannot escape its responsibility or escape penal action merely by filing a return showing an estimated income but without there being any real basis for that income.*"
>
> (underlining ours)

11. In that case the penalty was ultimately cancelled by this Court on the ground that there was no fraud or gross or wilful neglect on the part of the assessee and that the Tribunal's finding to the contrary was vitiated by failure to consider certain material facts.

12. We are bound by ratio of the decision of this Court. The number of discrepancies and irregularities listed by the special auditor in his report which are reproduced in the assessment order bear testimony to the fact that the books of accounts maintained by the assessee were wholly unreliable. If they were so, there can be no sanctity attached to the figure of gross contract receipts of Rs.20,30,74,024/- on which the assessee estimated 3% as its income. It is true that the assessing officer did not enhance the figure of gross receipts but that is not because he gave a clean chit to the books of accounts allegedly maintained by the assessee; he could not have given a clean chit in the face of the defects, discrepancies and irregularities reported by the special auditor. In order to take care of those discrepancies he resorted to a much higher estimate of the profits by adopting 11% on the gross contract receipts. He gave due opportunity to the assessee to explain the discrepancies and also to show why the profit rate of 11% cannot be adopted but these opportunities were not availed of by the assessee. He also has recorded in

the assessment order that the assessee was permitted to inspect the seized documents and was given photocopies of the desired documents (para 7). This is not denied by the assessee. In these circumstances, the mere fact that the estimate was reduced by the Tribunal to 8% would in no way take away the guilt of the assessee or explain its failure to prove that the failure to return the correct income did not arise from any fraud or any gross or wilful neglect on its part. It appears to us that the assessee was taking a chance – sitting on the fence - despite the fact that there was a search towards the close of the relevant accounting year in the course of which incriminating documents were found. It appears to us that the intention of the assessee was to take a risk and disclose a lesser income than what it actually earned and rely upon the minor variations in the rate of profits adopted by the taxing authorities and the Tribunal as a defence in the penalty proceedings. The plea – accepted by the Tribunal – that the assessee agreed to be assessed at 11% of the gross receipts only "to buy peace" and "avoid litigation" cannot be accepted by us in view of the judgment of the Supreme Court in *MAK Data P. Ltd.* (*supra*). The Tribunal in our view was in error in upholding the order of the CIT (Appeals) cancelling the penalty. We accordingly answer the substantial questions of law framed by us against the assessee and in favour of the revenue.

13. The appeal of the revenue is allowed with no order as to costs.

(R.V. EASWAR)
JUDGE

(S. RAVINDRA BHAT)
JUDGE

APRIL 15, 2014
hs