

S. N. Namasivayam Chettiar

Vs

Commissioner of Income-Tax, Madras

Civil Appeals Nos. 218 to 223 of 1955

(M. Hidayatullah, J. L. Kapur JJ)

03.02.1960

JUDGMENT

KAPUR, J. –

In these six appeals the common question raised is whether the proviso to section 13 of the Income-tax Act is applicable to the facts and circumstances of these cases. They are therefore disposed of by the judgment. Civil Appeal No. 218 of 1955 arises out of the assessment for the year 1943-1944. Civil Appeals Nos. 219 to 223 relate to the assessment year 1944-1945, 1946-47 and for the chargeable accounting periods from January, 1943, to February, 1944, and from February, 1945, to February, 1946. The appellant in each of the appeals is the assessee and the respondent is the Commissioner of Income-tax and Excess Profits Tax, Madras.

The appellant is a "resident and ordinarily resident" in India and carried on extensive trade in Colombo in grains, fodder, gram and other food - stuffs for cattle and poultry. For the assessment year 1943-1944, the appellant showed a turnover of Rs. 17,74,825 and a gross profit of Rs. 63,217 which is about 3.5 per cent. For the two previous assessment years the appellant's gross profits were 9 per cent. and 8 per cent. respectively. The Income-tax Officer, by his order dated March 20, 1948, rejected the accounts and estimated the gross profit by adding back Rs. 2,38,831 to the returned income. Thus he raised the turnover to Rs. 20,00,000 and the gross income to Rs. 3,00,000 giving a profit of 15 per cent on the estimated turnover. On appeal to the Appellate Assistant Commissioner, the order of the Income-tax Officer was confirmed. The Income-tax Appellate Tribunal on appeal by its order dated September 14, 1951, after pointing out various defects, rejected the account books but accepted the appellant's turn

"(1) Whether under the circumstances of the case the Tribunal was justified in holding that section 13 of the Indian Income-tax Act applies to the case ?

(2) Whether the reasons set out by the Appellate Tribunal in paragraph 2 of its judgment are sufficient to invoke section 13 of the Act ?

(3) Whether the Tribunal, having disagreed with the Department on the basis of the assessment had jurisdiction to apply section 13 and make an assessment on an alleged estimate ?

(4) Whether the Tribunal was justified in making an assessment on the basis of section 13 without giving an adequate opportunity to the assessee to meet the materials upon which eventually the assessment was rested ?"

But the Tribunal, by its order dated February 12, 1950, held that no question of law arose and therefore declined to state a case and thus rejected the application. The appellant then applied to the High Court of Madras under section 66(2) of the Act on the same four questions of law. This application was dismissed by the High Court on February 26, 1953. Against this order the appellant applied for special leave to appeal and, by leave of this court, amended the petition so as to make it an appeal against the order of the High court as well as the order of the Tribunal dated September 14, 1951.

In the other appeals also the course of proceedings before the Income- tax Officer, the Appellate Assistant Commissioner and the Income-tax Appellate Tribunal was the same. For the assessment years 1944-1945 and 1946-1947 the appellant disclosed a turnover of Rs. 10,35,748 and Rs. 5,98,728 respectively and the gross profits rates were 10.7 per cent. and 8.7 per cent. respectively. As the books of accounts in regard to these years also were rejected, the Income-tax Appellate Tribunal applied section 13 and estimated the gross profit rates at 12 1/2 per cent. and 10 per cent. for the respective years. The appellant applied to the Tribunal under section 66(1) of the Act for stating a case to the High Court for its decision on the following two points :

"(1) Whether on the facts and in the circumstances of the case, the Department was right in acting under the proviso to section 13 of the Act in the absence of a finding that income, profits and gains cannot properly be deduced from the books produced or that no method of accounting has been regularly employed ?

(2) Whether on the facts and in the circumstances of the case, the Department had sufficient materials before it to justify the rates of 12 1/2 per cent. and 10 per cent. gross profits on the total turnover on the ground that the rates worked out by the figures submitted by the assessee work out at a lesser figure ?"

The Tribunal dismissed the application on January 15, 1954. The appellant did not apply to the High Court under section 66(2) of the Income-tax Act but obtained special leave from this court against the order of the Tribunal by which it applied the proviso to section 13 of the Income-tax Act. All the six appeals were heard together and a common question arises whether the Income-tax Appellate Tribunal was justified in applying the proviso to section 13 of the Income-tax Act.

It was contended by the appellant in Civil Appeals Nos. 218, 219 and 221 of 1955 that the Income-tax Appellate Tribunal was not justified in applying the proviso to section 13 and assuming that the proviso did apply then the percentage worked out was unjustified and had been arrived at by relying upon material which the appellant had no opportunity to meet and therefore the case fell within the rule in *Dhakeswari Cotton Mills Ltd. v. Commissioner of Income-tax* where similar violation of the fundamental rule of natural justice - i.e., the information upon which the Tribunal relied was not disclosed to the assessee and no opportunity was given to him to rebut such material - was held to be a ground for interference with the order of the Tribunal.

It was rightly argued that the power to compute profits under the proviso to section 13 arises only where no method of accounting has been regularly employed by the assessee and where the method employed is such that the income, profits and gains cannot properly be deduced therefrom. It means that the method adopted by the assessee must prima facie prevail where it is regularly employed, though the Income-tax Officer can resort to the proviso if the method is such that true profits cannot be correctly determined therefrom. In other words, even if the assessee has regularly employed a method of accounting it can be discarded under the proviso if the method does not show correct

profits of the year.

The Appellate Tribunal, by its order dated September 14, 1951, held that correct profits could not be deduced from the books produced by the assessee and therefore the proviso to section 13 of the Income-tax Act applied. The reasons it gave were (1) that vouchers for several purchase made in Colombo had not been produced and for purchases of over Rs. 3,00,000 no vouchers were forthcoming and without the vouchers the entries in the account books could not be verified; (2) there was no quantitative tally for the grains and for other materials purchased by the appellant, which were ground into powder, turned into fodder, packed in different sized and then sold. It was not possible, according to the Tribunal, to accept the books of account, where the turnover was as large as about seventeen lakhs of rupees, without a quantitative tally;

(3) fairly big sum of money was alleged to have been paid towards purchasing of licenses for export from India; and Rs. 19,000 worth of purchases were made in Tuticorin when only a small sum of money in cash was shown in the assessee's accounts; (4) several outsiders' cheques had been entered in the accounts of the assessee without any proof as to why those cheques were paid to the assessee; and (5) a fairly big sum of money had been invested in India in the purchase of property without money being received from Colombo. On these facts the Tribunal said :

"In view of these defects, we are clearly of opinion that the correct profit could not be deduced from the books produced by the assessee, and accordingly hold that the proviso to section 13 of the Act applies in this case. The question, therefore, is regarding the estimate."

After giving this finding the Tribunal accepted the turnover as shown in the appellant's books. In making the computation of profits the Tribunal took into consideration the following matters : that the export of food grain from India was prohibited except under a licence, that there was an acute shortage of cattle fodder in Ceylon and the appellant had to resort to dubious means in order to obtain grains, that during a substantial portion of the year of accounting there was no price control in Colombo, that as the appellant was a manufacturer of forage by mixing several kinds of grains and powdering them and sold them in packets of various weights, the appellant must have made higher profits than persons who deal in grain only. Keeping all this in view the Tribunal was of the opinion that the rate of 15 per cent. adopted in regard to imported grains was not too high but in the case of local purchases it was, and therefore reduced the rate of profits in the latter case to 12 1/2 per cent. It was on this matter

On the basis of this remark it was argued that the principle of natural justice had been violated in that the Tribunal had taken into consideration the rate of profit in other cases without giving an opportunity to the appellant to explain those cases and relied upon *Dhakeswari Cotton Mills Ltd. v. Commissioner of Income-tax*, where a violation of the fundamental rule of justice, i.e., where the information was not disclosed to the assessee and no opportunity was given to rebut that material, was held to be a ground for interference with the order of the Tribunal. In our opinion, no such case arises in the present appeal. No information, as in *Dhakeswari's* case, was supplied to the Tribunal by any one and taken into consideration by it, and, therefore, it was not necessary to give and such opportunity as the appellant contends for. In the present case the Tribunal has held that from the method of accounting adopted by the appellant correct profits could not be deduced because of the various reasons which have

As a matter of fact, the Income-tax Officer who also rejected the accounts of the appellant had also given similar reasons. He had held that there was absence of vouchers, that the stock account and the manufacturing account had not been kept or produced, that the cheques of other parties had been credited in the accounts of the appellant which had not been explained and that there was purchase of goods and property by the appellant without the being sufficient case in hand. The Income-tax Officer also said that in other cases where grains were purchased in India and sold in Colombo the rates of profit were higher, ranging between 20 per cent. and 39 per cent. He then worked out profits in respect of various grains in the case of the appellant and found that the average rate of gross profit worked out to 15.8 per cent., and in his opinion the gross profit in fodder should have been higher. He further took into consideration the fact that Colombo was boomed in April, 1942, resulting in panic in that town and

It may be mentioned that throughout in his grounds of appeal the appellant has emphasised the inapplicability of section 13 of the Income-tax act and the proviso thereto, but not to this particular violation of principles of natural justice which was emphasised and particularised before us. In his appeal to the appellate Assistant commissioner no objection was taken to the reference by the Income-tax Officer to the rates of profit made by other dealers in grains. In the grounds of appeal to the Tribunal also there was no such objection. In the application under section 66(1) there was no specific ground taken and in the application under section 66(2) the matter does not seem to have been raised. The order of the High court, dated February 26, 1953, does not show that any such question was raised before it; all it shows is that the appellant's books of account were found to be defective and afforded no data for arriving at correct profits of the business. The order also refers to the non-production of invoice

It was then urged that the four reasons given, which we have set out above, could not make section 13 applicable. For the rejection of accounts several reasons were given by the Appellate Tribunal; one of these reasons was the non-production of stock registers and manufacturing accounts. This reason was given by the Income-tax Officer and adopted by the appellate Tribunal. It was submitted that the non-production of stock account was not such a defect as to entitle the taxing authorities to reject the books and apply the proviso to section 13. Reliance was placed on the judgment of the Punjab High Court in *Pandit Bros. v. Commissioner of Income-tax*. The acts in that case were very different. The Income-tax Officer there added a certain sum to the assessee's profits on the ground that the expense ratio was too high and the profits disclosed were too low and there was no stock register. The finding in that case was that the assessee maintained regular accounts of his purchases and sales and there was no finding

"There is no finding that there was material before the Income-tax Officer to lead him to the conclusion that a proper statement of income, profits and gains could not be deduced from the material placed before him. All he said was that the profits appeared to be somewhat low and there was no stock register."

The want of a stock register was, in that particular case, not a very serious defect because the account books had been found and accepted as correct and disclosed a true state of affairs. It cannot, therefore, be said that that case laid down as a proposition of law that the want of a stock register by which a proper check could be made was not such a serious defect as to make the proviso to section 13 in applicable.

The importance of such a register was pointed out by the Nagpur High Court in *Ghanshyamdas Permanand v. Commissioner of Income-tax*. In cases such as the instant case, the keeping of stock

register is of great importance because that is a means of verifying the assessee's accounts by having a "quantitative tally". If, after taking into account all the materials including the want of a stock register, it is found that from the method of accounting the correct profits of the business are not deducible, the operation of the proviso to section 13 of the Income-tax Act would be attracted, *Bombay Cycle Stores Co. Ltd. v. Commissioner of Income-tax*. It may also be added, as was held by this court in *Commissioner of Income-tax v. McMillan & Co.*, that the Income-tax Officer, even if he accepts the assessee's method of accounting, is not bound by the figure of profits shown in the accounts. It is for the Income-tax authorities to consider the material which is placed before them and, if, after taking into account in an

In regard to the Appeal No. 220 of 1955, for the assessment year 1946- 1947, the objection raised was that the Tribunal had committed the same error in that it took into consideration the earlier decision of the Tribunal "in an identical situation", i.e., in the case of the same assessee in regard to previous years. As we have held that there was no error in the order of the Tribunal in regard to the previous years, it cannot be said that this observation of the Tribunal was in any manner erroneous. This appeal should therefore be dismissed.

The other appeals which arise under the Excess Profits Tax Act for the various chargeable accounting periods depend upon the result of the income-tax assessment appeals and, as we have dismissed those appeals, these appeals also must be dismissed.

In the result all the six appeals are dismissed with costs. As the appeals were consolidated there will be one set of costs.

Appeals dismissed.

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