COMMISSIONER OF INCOME TAX, MADRAS

v.

M/S. KHODAY ESWARSA & SONS

September 22, 1971

[C. A. VAIDIALINGAM AND P. JAGANMOHAN REDDY, JJ.]

Income-tax Act (11 of 1922), s. 28(1)(c)—Levy of penalty—Reasons in assessment proceedings—Weight to be attached to.

In income-tax proceedings to the taxable income shown by the respondent in its return two items among others were added on the basis that there were illicit sales of alcohol and that certain sales had not been properly accounted for. Thereafter, the Income-tax Officer, Special Investigation Circle, issued notice that he proposed to levy a penalty under s. 28(1)(c) of the Income-tax Act, 1922, as the respondent had concealed particulars of its income and deliberately furnished inaccurate particulars. He rejected the explanation of the assessee and levied a penalty. In the order levying penalty the Income-tax Officer stated that the reasons for adding the disputed amounts in the total income of the assessee had been already discussed in the original order of assessment and that there was no need to repeat them. The Appellate Assistant Commissioner in appeal confirmed the penalty. His approach to the case was not different and was based upon a guess that because there were many contiguous dry areas the respondent would have surreptitiously sold alcohol. The Appellate Tribunal considered the circumstances under which the additions came to be made by the Department in the assessment proceedings, and the various points which were pressed before it and the Appellate Assistant Commissioner on behalf of the assessee, and held that though there might be certain doubtful transactions it could not be stated that assessee had made any deliberate attempt at concealment regarding its pharmaceutical section, and that, though there might be justification for making additions in the original assessment order those additions by themselves could not lead to the conclusion that the respondent had concealed its income or that it had furnished deliberately inaccurate particulars. On the basis of those findings the Appellate Tribunal set aside the order levying penalty. Thereafter, the Appellate Tribunal, holding that the reasons given by it for setting aside the penalty proceedings were all based on findings of fact and that no question of law arose out of those findings, rejected an application by the appellant for referring the question as to whether the Appellate Tribunal was right in cancelling the penalty. The appellant then filed an application under s. 66(2) of the Act but the High Court dismissed it on the same ground.

Dismissing the appeal,

HELD : The penalty proceedings being penal in character the Department must establish that the receipt of the amount in dispute constitutes income of the assessee. Apart from the falsity of any explanation given by the assessee the Department must have before it, before levying a penalty, cogent material or evidence from which it could be inferred that the assessee had consciously concealed the particulars of his income or had deliberately furnished inaccurate particulars. The original assessment proceeding for computing the tax is evidence in the penalty proceeding, but the penalty cannot be levied solely on the basis of the reasons given in the original assessment order. [853 B-D]

A In the present case, except the reasons given in the original assessment order for including the disputed items in the total income, the Department had no other material or evidence from which it could be reasonably inferred that the assessee had consciously concealed particulars of his income or had deliberately furnished inaccurate particulars. The Appellate Tribunal made a correct and judicial approach in considering the question whether the penalty provisions were attracted as against the respondent. The conclusions drawn by the Appellate Tribunal were findings of fact recorded against the Department. Since on those findings of fact no question of law arose the High Court was justified in rejecting the application filed by the appellant under s. 66(2) of the Act. [852 B-E] 853 E-F]

*Commissioner of Income-tax West Bengal-*1 v. *Anwar Ali,* [1970] 76 I.T.R. 696, followed.

C CIVIL APPELLATE JURISDICTION : Civil Appeal No. 648 of 1967.

Appeal by special leave from the judgment and order dated October 3, 1966 of the Mysore High Court in Civil Petition No. 10 of 1966.

D *R. H. Dhebar* and *J. Ramamurthi,* for the appellant.

The respondent did not appear.

The Judgment of the Court was delivered by

Vaidialingam, J. This appeal, by special leave, by the Commissioner of Income-tax, Madras, is against the judgment and E order dated October 3, 1966 of the High Court of Mysore, rejecting the appellant's application filed under s. 66(2) of the Income-tax Act, 1922 (hereinafter to be referred as the Act) for directing the Income-tax Appellate Tribunal, Madras Bench to refer the question of law to the High Court.

The question of law, which the appellant wanted to be referred F was :

> "Whether on the facts and in the circumstances of the case the Appellate Tribunal was right in cancelling the penalty of Rs. 35,000 levied under section 28(1)(c) of the Indian Income-tax Act, 1922."

G The respondent was a firm carrying on business of manufacturing silk, carbon papers, type-writer ribbons, liquor, spirituous drugs and chemicals etc. In respect of the assessment year 1955-56, the respondent had sent a return showing Rs. 51,214 as taxable income. On looking into the accounts and other records, the Income-tax Officer made several additions to the amount shown in the return and ultimately fixed the total assessable income in H the sum of Rs. 3,30,474. On appeal, the amount was reduced and the taxable income was fixed in the sum of Rs. 2,09,575. In the further appeal by the assessee to the Appellate Tribunal, there

was no alteration in this figure. Only two items which were added to the income and which have been accepted by all the authorities required to be noticed. They are :

Pharmaceuticals, section—Rs. 77,518.00

Chemicals section—Rs. 9,900.00.

Relating to the pharmaceuticals section, it is the view of the Income-tax Officer that some of the sale bills produced by the respondent were found to be forged ones and some of the purchasers of tincture were also fictitious persons. There was no evidence produced by the assessee to show that the Kolae powder, which was very essential for the manufacture of tincture had been purchased by it. Hence the Income-tax Officer drew an inference that the respondent had not really manufactured tincture and that on the other hand the firm must have sold all alcohol illicitly.

It was on this basis that the Income-tax Officer held that the assessee must be considered to have omitted to show the sum of Rs. 77,588. Similarly, regarding chemical section, the Income-tax Officer found that the respondent has not accounted for a part of sale of Ethyl Acetate and that on verification it was found that there has been a large deficit of rectified spirit. On this basis the Income-tax Officer drew an inference that the firm has again secreted a large quantity of rectified spirit under the cloak of manufacture of chemicals. On the ground that certain sales had not been properly accounted for, the sum of Rs. 9,900 was added to the taxable income of the assessee. It was on the above basis that the two items were included in the total assessable income of the assessee firm.

These reasons given by the Income-tax Officer have been, by and large, accepted by the Appellate Assistant Commissioner and the Income-tax Appellate Tribunal. The Income-tax Officer, Special Investigation Circle A, Bangalore issued a notice under s. 28(1) to the respondent that it has concealed the particulars of its income and deliberately furnished inaccurate particulars in respect of the above amounts added to the total income and that the Income-tax Officer proposed to levy a penalty under s. 28 (1)(c) of the Act. No doubt, in the notice certain other items, which had already been added to the total income were also referred to. But those items have been deleted from the penalty proceedings by the Appellate Assistant Commissioner. Therefore, we are only concerned with the two items, referred to earlier.

The assessee sent a reply stating that it has not concealed the particulars of its income nor has it deliberately furnished inaccurate particulars of such income. The explanation offered by the assessee was not accepted by the Income-tax Officer, and the latter

A by his order dated February 15, 1963 imposed a penalty of Rs. 35,000 on the ground that the respondent had concealed the particulars of its income. That amount of penalty was levied by the Income-tax Officer on the ground that over and above the two items relating to the Pharmaceuticals and Chemical sections, there has been a concealment of three more items totalling Rs. 32,267.
B They were :

Silk business; shortage in twisted silk yarn	Rs. 14,545.00
Shortage in Artificial silk	Rs. 3,434.00
Carbons; Unaccounted consumption	Rs. 14,288.00

C It was on this basis that the total penalty was levied.

On appeal to the Appellate Assistant Commissioner, the latter, no doubt deleted these three items totalling Rs. 32,267 from the penalty proceedings, but confirmed the order of the Income-tax Officer regarding the two other items holding that the omission by
D the assessee to include the said two items amounted to the firm concealing particulars regarding its income under s. 28(1)(c) of the Act. The penalty amount levied by the Income-tax Officer was also confirmed. Though the Appellate Assistant Commissioner reduced the quantum of concealment—even assuming that there has been a concealment—he did not make any reduction
E in the penalty actually levied by the Income-tax Officer.

The assessee carried the matter in appeal before the Income-tax Appellate Tribunal, Madras Bench. The main grievance made by the assessee was that there has been no independent consideration by the Income-tax Officer or the Appellate Assistant Commissioner whether even on the basis that there has been an omis-
F sion by it to include certain items in its return, such omission came within s. 28(1)(c) of the Act, so as to attract the levy of penalty. The assessee also contended that both the Income-tax Officer and the Appellate Assistant Commissioner have mainly relied on the reasons given in the order of assessment for adding these two items in the total income. According to the assessee there
G has been no proper exercise of jurisdiction under s. 28 of the Act.

The Income-tax Appellate Tribunal by its order dated November 13, 1964 set aside the order of the Income-tax Officer as confirmed by the Appellate Assistant Commissioner levying penalty
H on the respondent.

The Commissioner of Income-tax filed an application under s. 66(1) of the Act, requiring the Appellate Tribunal to draw up

a statement of the case and refer the question extracted in the earlier part of the judgment, to be referred to the High Court. The Appellate Tribunal by its order dated June 7, 1965 rejected the said application on the ground that the reasons given by it for setting aside the penalty proceedings were all based on findings of fact and that no question of law arose out of those findings.

The appellant filed an application before the High Court of Mysore, under s. 66(2) for directions being issued to the Appellate Tribunal to state the case and refer the question of law, which the Appellate Tribunal has refused to refer. A Division Bench of the High Court by its order dated October 3, 1966 dismissed the appellant's application on the ground that the finding of the Appellate Tribunal that the Income-tax Department had failed to prove that the assessee had concealed its income or that it had deliberately furnished inaccurate particulars of its income are all on facts and that no question of law arises from the order of the Appellate Tribunal.

Mr. Dhebar, learned counsel for the appellant, urged that the order of the High Court is erroneous. According to him the view of the High Court that the conclusions arrived at by the Appellate Tribunal are all on facts and that no question of law arises, is erroneous. The counsel urged that there has been an omission by the respondent to include in particular two items which are the subject of penalty proceedings and the order of assessment in that regard has become final. Hence it follows that this is a case where the assessee has concealed the particulars of its income or has deliberately furnished inaccurate particulars of its income. Both the Income-tax Officer as well as the Appellate Tribunal have in the penalty proceedings gone elaborately into this aspect before levying penalty. The approach made by the Appellate Tribunal when it set aside the orders levying penalty is not justified in law. Therefore, he urged that the High Court should have directed the Appellate Tribunal to state a case and refer the question of law as prayed for by the Appellant.

The respondent has not entered appearance before us. We have been taken through the entire proceedings leading up to the order levying penalty. We have also gone through the reasons given by the Income-tax Officer for levying penalty as well as the order of the Appellate Assistant Commissioner confirming the same. We cannot accept the contention of Mr. Dhebar that the Appellate Tribual has summarily interfered with the orders levying penalty. We have gone through the order of the Appellate Tribunal and we find that it has considered the circumstances under which the additions came to be made by the Department in the assessment proceedings as well as the points that were pressed before it, on behalf of the assessee as well as the Appelate Assistant

A Commissioner. It is the view of the Appellate Tribunal that the Department has not established that the assessee has not manufactured tincture and that it had sold only alcohol. This conclusion arrived at by the Income-tax Officer in the penalty proceedings is, according to the Appellate Tribunal, purely one of conjecture or surmise. The Appellate Tribunal, no doubt, was prepared to B accept the contention of the Department that there were a lot of doubtful circumstances. Notwithstanding these circumstances the Appellate Tribunal is of the view that when admittedly there are Excise authorities in the premises of the respondent, it is very difficult to hold that those officers would have permitted the assessee to utilise the alcohol for other purposes. The Appellate Tribunal C has also held that even the sale bills produced by the respondent, contain the proper permit numbers given by the Excise authorities and that the Income-tax Department have not made any inquiries from the Excise authorities whether those relevant sales have been made without their authorisation. The Appellate Tribunal has further held that there is no stock discrepancy in Kola Liquidum D if the transactions are considered as a whole for the entire period. Therefore, regarding Pharmaceuticals section the Appellate Tribunal finally held that though there may be certain doubtful transactions, it cannot be stated that the assessee has made any deliberate attempt at concealment. Regarding the Chemical section, the Appellate Tribunal is of the view that though there may be justification for making additions in the original assessment order to the amount E shown in the return, those additions by themselves cannot lead to the conclusion that the respondent has concealed its income or that it has furnished deliberately inaccurate particulars.

It was on the basis of these findings that the Appellate Tribunal has set aside the order levying penalty.

F

One thing that strikes us when going through the order of the Income-tax Officer levying penalty and the order of the Appellate Assistant Commissioner confirming the said levy, is that there is not much of an independent discussion regarding the material question that has to be considered, namely, whether the firm has G concealed the particulars of its income or whether it has deliberately furnished inaccurate particulars of such income. On the other hand, the Income-tax Officer after refering to the explanation furnished by the assessee to the show cause notice, clearly says that the facts relating to the unaccounted items have been fully discussed already in the relevant assessment orders for the concerned assessment year and that the reasons given therein need not be repeated H again. Then there is only a very summary disposal of the plea raised by the respondent that he has not concealed the particulars of his income, nor has it delibertely furnished inaccurate particulars

of its income. The approach made by the Appellate Assistant Commissioner is not far different from that of the Income-tax Officer. In fact the Appellate Assistant Commissioner makes a further guess that in view of the fact that there were very many dry areas bordering Mysore, the respondent would have surreptitiously sold alcohol that was supplied to it without using it for the purpose of making tincture. It is the view of the Appellate Assistant Commissioner that the mere fact that there are Excise authorities to control the activities of persons like the assessee, is of no material consequence. From what we have stated above, it is clear that while there has been no proper approach made by either the Income-tax Officer when he levied penalty or by the Appellate Assistant Commissioner when he confirmed the order levying penalty, the Appellate Tribunal, on the other hand, has made a very correct and judicial approach in considering the question whether the penalty provisions are attracted as against the respondent. After a very fair and full consideration of the material circumstances, the Appellate Tribunal has set aside the order levying penalty. As rightly pointed out by the High Court, the conclusions drawn by the Appellate Tribunal are all on findings of fact recorded against the Department. On those findings of fact, there was no question of law arising for reference being made to the High Court. Under those circumstances, the High Court was perfectly justified in rejecting the application filed by the appellant under s. 66(2) of the Act.

Before we conclude we may refer to the decision of this Court in *Commissioner of Income-tax West Bengal I, and Another* v. *Anwar Ali*[1], wherein it has been held that one of the principal objects in enacting s. 28 is to provide a deterrent against recurrence of default on the part of the assessee and that s. 28 is penal in the sense that its consequences are intended to be effective deterrent which would put a stop to the practices which the legislature considers to be against the public interest. It has been further held that the Department must establish that the receipt of the amount in dispute constitutes the income of the assessee and if there is no evidence on record except the explanation given by the assessee, which explanation has been found to be false, it does not follow that the receipt constitutes its taxable income. It has been further held that as the proceedings under s. 28 are of a penal nature and the burden is on the Department that a particular amount is revenue receipt, it is legitimate to say that the mere fact that the explanation of the assessee is false, does not necessarily give rise to the inference that the disputed amount represents the income. It has been pointed out in the said decision that the finding given in the assessment proceeding for determining or computing the tax is not conclusive

[1] [1970] 76 I.T.R. 696.

A though it may be good evidence. It has been further held by this Court in the above decision :

> "Before penalty can be imposed the entirety of circumstances must reasonably point to the conclusion that the disputed amount represented income and that the assessee had consciously concealed the particulars of his
B income or had deliberately furnished inaccurate particulars."

From the above it is clear that penalty proceedings being penal in character, the Department must establish that the receipt of the amount in dispute constitutes income of the assessee. Apart from
C the falsity of the explanation given by the assessee, the Department must have before it before levying penalty cogent material or evidence from which it could be inferred that the assessee has consciously concealed the particulars of his income or had deliberately furnished inaccurate particulars in respect of the same and that the disputed amount is a revenue receipt. No doubt the original assessment proceedings, for computing the tax may be a good item
D of evidence in the penalty proceedings; but the penalty cannot be levied solely on the basis of the reasons given in the original order of assessment.

In the case before us we have already pointed out that in the order levying penalty the Income-tax Officer has categorically stated
E that the reasons for adding the disputed amounts in the total income of the assessee have been already discussed in the original order of assessment and that they need not be repeated again. The Appellate Assistant Commissioner, we have already pointed out, has made only a guess work. That clearly shows that except the reasons given in the original assessment order for including the disputed items in the total income, the Department had no other material
F or evidence from which it could be reasonably inferred that the assessee had consciously concealed the particulars of his income or had deliberately furnished inaccurate particulars.

For all the reasons given above, it follows that there is no merit in the appeal and it is accordingly dismissed. As the respondent
G has not appeared, there will be no order as to costs.

V.P.S. *Appeal dismissed.*