



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

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Judgment reserved on: 13 February 2024
Judgment pronounced on: 01 March 2024

+ ITA 862/2019

PR. COMMISSIONER OF INCOME TAX (CENTRAL) -1

..... Appellant

Through: Mr. Zoheb Hossain, SSC and
Mr. Sanjeev Menon, JSC

versus

M/S FORUM SALES PVT. LTD. Respondent

Through: Mr. Yoginder Handoo and Mr.
Ashwin Kataria, Advs.

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CORAM:

HON'BLE MR. JUSTICE YASHWANT VARMA

HON'BLE MR. JUSTICE PURUSHAINDRA KUMAR

KAURAV

J U D G M E N T

PURUSHAINDRA KUMAR KAURAV, J.

1. These appeals under Section 260A of the Income Tax Act, 1961

["Act"] are filed at the instance of the Revenue, against the common

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order of the Income Tax Appellate Tribunal [“ITAT”] dated 22.10.2018 for the Assessment Years [“AY”] 2013-14 and 2014-15. For the sake of convenience, the facts are taken from ITA 862/2019.

2. The respondent-assessee in the instant case is a company which deals in gift items and novelties, pet treat products, market survey and research and commission business and engaged in providing corporate gifting solutions to various companies. A search, seizure and survey operation under Section 132/133A of the Act was conducted on 15.02.2014 on the AMQ group of companies including the office premises of the respondent-assessee. Consequently, a notice under Section 153A of the Act was issued to the respondent-assessee for filing its income tax return [“ITR”] for six preceding years from the date of search i.e., for the years 2008-09 to 2013-14.

3. On 30.11.2014, the respondent-assessee filed its ITR declaring income of Rs.66,53,882/- for AY 2014-15. A notice under Section 143(2) of the Act was issued on 10.09.2015 and another notice under Section 142(1) of the Act alongwith detailed questionnaire was subsequently issued on 06.09.2016 to the respondent-assessee.

4. Thereafter, on 27.12.2016, the Assessing Officer [AO] passed an order under Section 143(3) of the Act, assessing the income of the respondent-assessee at Rs.11,11,66,320/- by making the following additions in the total income for the concerned AY:

- i. Addition of Rs.42,53,909/- on account of estimation of unaccounted profit.



- ii. Addition of Rs.19,05,653/- on account of disallowance of expenses.
- iii. Addition of Rs.9,30,49,222/- on account of inflated purchases.
- iv. Addition of Rs.51,72,955/- on account of deemed dividend under Section 2(22)(e) of the Act.
- v. Addition of Rs.1,00,000 on account of cash found and seized.

5. Being aggrieved by the order of the AO, the respondent-assessee preferred an appeal before the Commissioner of Income-Tax (Appeals) [“CIT (A)”], who *vide* order dated 28.02.2018 partly allowed the appeal of the respondent-assessee. The CIT (A), while considering the fact that the AO has failed to raise any objection *qua* the genuineness of the books of account which were duly audited by the auditor, deleted the additions of Rs.19,05,653/- on account of disallowance of expenses and Rs.9,30,49,222/- on account of inflated purchases. The CIT (A) also held that the addition of Rs.1,00,000 on account of cash found and seized was made on the protective basis and in view of the substantive addition already made in the hands of Mr. Moin Akhtar Qureshi, which was mentioned by the AO, the said addition should be deleted.

6. Thereafter, the respondent-assessee as well as the Revenue preferred cross appeals before the ITAT. The ITAT dismissed the appeal of the Revenue and partly allowed the appeal of the respondent-assessee. The issue pertaining to the addition based on estimation of unaccounted profits was remitted back to the AO with a direction to obtain information from the parties regarding transactions carried on by the respondent-assessee during the concerned AYs. The ITAT further



upheld the findings of the CIT (A) on the additions made in respect of disallowance of expenses and inflated purchases of Rs.19,05,653/- and Rs.9,30,49,222/-, respectively, in absence of any defect on record brought by the AO. Without finding any infirmity in the order of the CIT (A), the ITAT held that neither the AO had endeavoured to make any further query to examine the genuineness of the expenses, nor he had made any specific remark with respect to any defect in maintaining the details by the respondent-assessee.

7. The Revenue in the instant petition has, therefore, proposed the following questions of law for our consideration:

A. Whether, in the fact and circumstances of the case, the ITAT was justified in law in deleting addition of Rs.42,53,909/- made by the AO on account of unaccounted profits based on seized documents?

B. Whether, in the fact and circumstances of the case, the ITAT was justified in law in deleting addition of Rs.19,05,653/- made by the AO on account of disallowance of expenses?

C. Whether, in the facts and circumstances of the case, the ITAT was justified in law in deleting the addition of Rs.9,30,49,222/- made by the AO on account of inflated purchases?

D. Whether, in the fact and circumstances of the case, the ITAT was justified in law in deleting the protective addition of Rs.1,00,000/- added on account of cash found and seized?

E. Whether, in the fact and circumstances of the case, the ITAT was justified in law in deleting the addition made by the AO on



account of deemed dividend by not appreciating that Section 2(22)(e) of the Act excludes the transaction of lending money in only two circumstances i.e., firstly if the company is in the business of money lending and secondly if the payment is made in the ordinary course of the business and the alleged ad-hoc money lending to its group companies in the case of the assessee does not come in the ambit of the exclusion contained in the said provision?

F. Whether, in the fact and circumstances of the case, the ITAT was justified in law by not appreciating that the provision of Section 2(22)(e) of the Act creates a legal fiction whereby any payment, by any company by way of advance or loan to a shareholder or to any concern in which such shareholder is a member or partner and in which he has a substantial interest is treated as dividend and the deeming fiction, upon; ingredients being satisfied has to be given effect?

G. Whether, in the fact and circumstances of the case, the ITAT was justified in law in deleting Rs.51,72,955/- added on account of deemed dividend under Section 2(22)(e) of the IT Act?

8. On 26.09.2019, notice was issued to the respondent-assessee in the instant case, which was duly accepted on the even date by the learned counsel for the respondent-assessee, who was present on advance notice.

9. Thereafter, on 21.07.2023, the matter was taken up for consideration and the order passed by this Court on the said date would



manifest that the appellants had conceded that the abovementioned questions (E), (F) and (G) stand covered against the appellants by virtue of the decision rendered by this Court in **CIT v. Ankitech (P) Limited** [2011 SCC OnLine Del 2213]. The order dated 21.07.2023 reads as under:-

- “1. This appeal concerns Assessment Year (AY) 2014-15.
2. The appellant/revenue has proposed seven (7) questions of law.
3. According to Mr Sanjeev Menon, learned standing counsel, who appears on behalf of the appellant/revenue, the proposed questions (e), (f) and (g) stand covered against the appellant/revenue, by virtue of the judgment rendered by a coordinate bench of this court in CIT v. Ankitech Pvt. Ltd., (2011) 11 taxmann.com 100 (Delhi).
4. We are informed that a Special Leave Petition (SLP) was preferred against the said judgment, which was also dismissed.
5. Learned counsel for the parties will file written submissions, not exceeding three (3) pages each, at least five (5) days before the next date of hearing, confined to the proposed questions (a) to (d).
6. List the matter on 24.01.2024.”

10. *Vide* another order dated 24.01.2024, this Court held as under:-

“2. It is thus manifest that since the exercise of assessment was not confined merely to the material gathered in the course of a search but was kept open to be examined with reference to all transactions in the Assessment Years in question, we find no ground to entertain the instant appeals on Question A.

3. We have by our earlier orders dated 21 July 2023 passed separately in both the appeals found that Questions E, F and G [in ITA No. 862/2019] and Questions D, E & F [in ITA No. 863/2019] would also not merit consideration as the same are covered against the appellant.”

11. It is thus seen that only questions (B), (C) and (D), as mentioned above, are left for adjudication and require consideration by this Court in the given facts and circumstances.

12. With respect to the questions (B), (C) and (D), learned counsel appearing on behalf of the Revenue submitted that the findings of the

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CIT (A) and the ITAT are *de hors* the settled position of law as the respondent-assessee had failed to substantiate the claims of the expenses with supporting documents, bills or vouchers which could legitimize the allowability of the expenses. According to him, the expenses claimed by the respondent-assessee are bogus/inflated expenses in order to substantially mitigate the taxable income and therefore, the additions made by the AO to the total income of the respondent-assessee do not suffer from any perversity, material illegality or arbitrariness.

13. The Revenue has relied upon the decision in the case of **Unit Construction Co. Ltd. v. Joint Commissioner of Income Tax** [2003 SCC OnLine Cal 756] to contend that it is not necessary for the AO to reject the books of account in order to assess the income on the best judgment basis. He has also placed reliance on the decision of this Court in the case of **Commissioner of Income-tax v. Paradise Holidays** [2010 SCC OnLine Del 1753].

14. Learned counsel for the respondent-assessee, on the other hand, vehemently opposed the arguments advanced by the appellant and submitted that the additions made by the AO are only based upon surmises and conjectures. According to him, the ledger containing the details of the parties alongwith their addresses was presented to the AO to explain the expenses, however, the AO did not make any effort to verify the genuineness of such expenses from the concerned parties. He further submitted that in the absence of any discrepancy in the books of account and more importantly, without rejecting the books of account,



such disallowance of the purchases by the AO is completely unjustified and contrary to the provisions of the Act. He, therefore, submitted that there were no cogent reasons to make the aforesaid additions at the behest of the AO and the view taken by the ITAT and CIT (A) in favour of the respondent-assessee is the correct enunciation of law.

15. Learned counsel has placed reliance on the decision of the Hon'ble Supreme Court in the case of **Sargam Cinema, Haldwani v. Commissioner of Income-tax, Haldwani** [(2010) 15 SCC 546], to contend that the books of account must have been rejected.

16. We have heard the learned counsel appearing on behalf of the parties and perused the record.

17. It is expedient to primarily advert to Section 145(3) of the Act which deals with the method of accounting and provides that in cases where the AO is not satisfied about the correctness or completeness of the accounts of the assessee, the assessment may be carried out in accordance with the procedure laid down in Section 144 of the Act. Section 145(3) of the Act reads as under:-

“145. Method of accounting—

(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.]”



18. For the sake of clarity, Section 144 of the Act, which prescribes the manner in which the best judgment assessment has to be completed by the Revenue, is culled out as under:-

“144. Best Judgment Assessment— (1) If any person

(a) fails to make the return required under sub-section (1) of Section 139 and has not made a return or a revised return under sub-section (4) or sub-section (5) [or an updated return under sub-section (8A)] of that section, or

(b) fails to comply with all the terms of a notice issued under sub-section (1) of Section 142 or fails to comply with a direction issued under sub-section (2-A) of that section, or

(c) having made a return, fails to comply with all the terms of a notice issued under sub-section (2) of Section 143,

the Assessing Officer, after taking into account all relevant material which the Assessing Officer has gathered, shall, after giving the assessee an opportunity of being heard, make the assessment of the total income or loss to the best of his judgment and determine the sum payable by the assessee on the basis of such assessment:

Provided that such opportunity shall be given by the Assessing Officer by serving a notice calling upon the assessee to show cause, on a date and time to be specified in the notice, why the assessment should not be completed to the best of his judgment:

Provided further that it shall not be necessary to give such opportunity in a case where a notice under sub-section (1) of Section 142 has been issued prior to the making of an assessment under this section.

(2) The provisions of this section as they stood immediately before their amendment by the Direct Tax Laws (Amendment) Act, 1987 (4 of 1988), shall apply to and in relation to any assessment for the assessment year commencing on the 1st day of April, 1988, or any earlier assessment year and references in this section to the other provisions of this Act shall be construed as references to those provisions as for the time being in force and applicable to the relevant assessment year.”

19. A plain reading of the aforementioned provisions would indicate that the AO wields an authority to make additions on the basis of

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estimation of income upon fulfillment of the conditions mentioned in Section 145(3) of the Act. Once the AO is satisfied about the existence of irregularities in the books of account as per Section 145(3) of the Act, it shall proceed in the manner provided under Section 144 of the Act. At this juncture, what needs consideration is the question whether such an addition must be made only after the rejection of the books of account by the AO.

20. The Division Bench of the High Court of Bombay in the case of **Principal Commissioner of Income-tax v. Swananda Properties Pvt. Ltd.** [2019 SCC OnLine Bom 13359] had an occasion to consider the said question and the same was accordingly answered as under:-

“11. We note that the books of account of the respondent were rejected by the Commissioner of Income-tax (Appeals) under section 145(3) of the Act. However, the Tribunal found in the impugned order that the invocation of section 145(3) of the Act is unjustified as no defect was noted in the books of account to disregard the same. We note that the Commissioner of Income-tax (Appeals) in his order while rejecting the books of account does not specify the defect in the record. The basis of the rejection appears to be best judgment of assessment done by him. **The rejection of the books should precede the best judgment assessment.** On facts, the Revenue has not been able to show any defect in the respondent's records which would warrant rejection of the books and making a best judgment assessment. Thus, on facts the view taken by the Tribunal is a possible view. Therefore, no substantial question of law arises. Thus not entertained.”

[Emphasis supplied]

21. The Division Bench of the Karnataka High Court in the case of **CIT v. Anil Kumar & Co.** [2016 SCC OnLine Kar 8512], has held that in cases where the Revenue had failed to reject the books of account and proceeded to an estimation of income without framing the assessment under Section 144 of the Act, such an action is

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unsustainable as per law. The relevant paragraph of the said decision is reproduced as under:-

“11. In so far as the estimation of gross profit made by the Assessing Officer modified by the Commissioner of Income-tax (Appeals), the Tribunal has rightly held that when the books of account of the assessee had not been rejected and assessment having not been framed under section 144 of the Income-tax Act the said authorities were in error in resorting to an estimation of income and such exercise undertaken by them was not sustainable. Section 145(3) of the Act lays down that the Assessing Officer can proceed to make assessment to the best of his judgment under section 144 of the Act only in the event of not being satisfied with the correctness of the accounts produced by the assessee. In the instant case the Assessing Officer has not rejected the books of account of the assessee. To put it differently the Assessing Officer has not made out a case that conditions laid down in section 145(3) of the Act are satisfied for rejection of the books of account. Thus, when the books of account are maintained by the assessee in accordance with the system of accounting, in the regular course of his business, the same would form the basis for computation of income. **In the instant case it is noticed that neither the Assessing Officer nor the Commissioner of Income-tax (Appeals) have rejected the books of account maintained by the assessee in the course of the business. As such the Tribunal has rightly rejected or set aside the partial addition made by the Assessing Officer for arriving at gross profit and sustained by the Commissioner of Income-tax (Appeals) and rightly held that the entire addition made by the Assessing Officer was liable to be deleted. The said finding is based on sound appreciation of facts and it does not give rise for framing substantial question of law.”**

[Emphasis supplied]

22. In another case of **Principal Commissioner of Income-tax v. Marg Ltd.** [2017 SCC OnLine Mad 37852], the Division Bench of the High Court of Madras has held that the rejection of books of account is *sine qua non* before the AO proceeds to make his own assessment. Paragraph 4(c) of the said decision is reproduced as under:-

“4(c). **Therefore, it is sine qua non that the Assessing Officer to come to a conclusion that the books of account maintained by the assessee are incorrect, incomplete or unreliable and reject the books of account before the proceeding to make his own assessment.** In the instant case,



there is no reference in the assessment order of the Assessing Officer regarding rejection of books of account.”

[Emphasis supplied]

23. In the case of **CIT v. Gian Chand Labour Contractors** [2007 SCC OnLine P&H 1577], the Division Bench of the High Court of Punjab and Haryana while taking a similar view, has held as follows:-

“8. Section 29 of the Act prescribes that the income referred to in section 28 which is assessable under the head “Profits and gains of business or profession” shall be computed in accordance with the provisions contained in sections 30 to 43A of the Act. Section 145 of the Act provides for computation of income under section 29 on the basis of books of account and the method of accounting regularly followed by the assessee. **However, where the Assessing Officer is not satisfied with the correctness or completeness of the said books, he may reject the same and estimate the income to the best of his judgment in accordance with the provisions of section 144 of the Act.** When an estimate is made to the best judgment of an Assessing Officer, he substitutes the income that is to be computed under section 29 of the Act. Once the best judgment assessment is made by fixing a rate of net profit, the assessee's claim for deduction on account of expenses cannot be deemed to have been ignored. The net profit rate is applied after taking into consideration all factors and it accounts for all the deductions which are referred to under section 29 and are deemed to have been taken into consideration while making such an estimate.”

[Emphasis supplied]

24. The series of judgments referred to hereinabove clearly allude to the settled position of law that the books of account have to be necessarily rejected before the AO proceeds to the best judgment assessment upon fulfilment of conditions mentioned in the Act. The underlying rationale behind such an action is to meet the standards of correct computation of accounts for the purpose of a more transparent and precise assessment of income. Therefore, any pick and choose method of rejecting certain entries from the books of account while

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accepting other, without an appropriate justification, is arbitrary and may lead to an incomplete, unreasonable and erroneous computation of income of an assessee.

25. In the present case, the ITAT has made a categorical finding that despite the fact that the AO was provided with the requisite bills, vouchers and addresses of the transacting parties, it did not make any effort to confirm the veracity of the alleged bogus or inflated bills.

26. We, hereby, also take note of the observations made by the ITAT in its order dated 22.10.2018 in Paragraph 25, wherein, while affirming the deletion of additions *vide* order of the CIT (A), it was held as under:-

“25. We find although the Assessing Officer was having complete address of the parties, however, he did not bother to call for any information from the said parties if he had some doubts. The entire addition by disallowing of 40% of the purchases in our opinion is not justified when the books of account are not rejected. We find the Hon'ble Gujarat High Court in the case of Yunus Haji Fazawala Vs. CIT (supra) has held that action of the Assessing Officer in disallowing 25% of purchases by doubting its genuineness without rejecting the books of account cannot be sustained. The order of the Tribunal confirming the disallowance was accordingly reversed. Since in the instant case also the books of account are not rejected, therefore, action of the CIT(A) in deleting such addition is justified. Further we find merit in the findings of the CIT (A) that if the action of the Assessing Officer is accepted then profit of the assessee will be 32.9% for A.Y. 2013-14 and 56.09% for A.Y. 2014-15 which is illogical and absurd. Since the order of the CIT(A) on this issue is just and proper under the facts and circumstances of the case, therefore; we do not find any infirmity in the same. Accordingly the same is upheld and the ground raised by the revenue is dismissed.”



27. Also, the decisions relied upon by the Revenue do not essentially support its case as the facts of the cited cases are strikingly different from the case at hand and therefore, the same are distinguishable. Though the decision of the Division Bench of the Calcutta High Court in *Unit Construction Co. Ltd.* would only have a persuasive value, however, a closer scrutiny of the same leads us to the conclusion that the said decision was rendered in the context of unexplained investments as per the scheme of Section 69 of the Act. In *Paradise Holidays*, the issue pertained to the rejection of books of account without an appropriate justification and therefore, unlike the present case, the challenge was laid with respect to the rejection of books of account itself.

28. So far as the proposed question (D) is concerned, the same is a matter of fact which has been settled by the ITAT which states that the action of the AO in making an addition of Rs.1,00,000/- on the protective basis, which already stood explained, deserved to be deleted. The ITAT further held that the substantive addition has already been made in the hands of Mr. Moin Akhtar Qureshi, which has been mentioned by the AO himself and therefore, there is no infirmity in deletion of the said addition by the CIT (A).

29. Admittedly, the addition of income as discussed in questions (B), (C) and (D) on estimate basis has been done without rejecting the books of account. In view of the aforesaid, we find that no substantial question of law arises in the present appeals.



30. Consequently, we do not find any merit in the case of the Revenue and have no reason to interfere with the view taken by the ITAT. Therefore, the appeals stand dismissed. Pending application(s), if any are also disposed of.

PURUSHAINdra KUMAR KAURAV, J.

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