IN THE HIGH COURT OF DELHI AT NEW DELHI

RESERVED ON: 28.09.2012
PRONOUNCED ON: 19.10.2012

\+ **ITA No. 58/2008**

COMMISSIONER OF INCOME TAX DELHI IV .... Appellant

Through: Sh. Sanjeev Rajpal, Sr. Standing Counsel.

versus

GOYAL M.G. GASES P. LTD. ..... Respondent

Through: Sh. C.S. Aggarwal, Sr. Advocate with Sh. Prakash Kumar, Advocate.

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

MR. JUSTICE S.RAVINDRA BHAT

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1. The following questions of law arise in this appeal:

"(i). Whether the ITAT was correct in law in deleting the penalty of Rs. 47,68,180/- imposed by the Assessing Officer u/s 271(c) of the Act?

(ii). Whether the ITAT was correct in law in deleting the penalty ignoring the material fact that the transaction was

treated as sham by ITAT as well as by this court (227 ITR 536) in the quantum proceedings?"

2. The assessee filed its return for the assessment year 1989-90 declaring an income of Rs. 23,74,987/-. The Assessing Officer by order dated 30.3.1992 assessed the assessee's income at Rs. 11,24,84,725/- which included disallowance of depreciation of Rs. 37,69,273/- on computers purchased by the assessee from Pertech Computers Ltd. (PCL, in short) and leased back to Altos India Pvt. Ltd. (Altos, in short); both the companies being under the same management. The CIT(A) through order dated 16.09.1992, and the Income Tax Appellate Tribunal (Tribunal, in short) through order dated 20.10.1993 confirmed the addition made by the AO by disallowing the depreciation on computers. In further appeal, this Court, through judgment dated 04.11.1996 confirmed the AO's disallowance, holding that the findings recorded by the Tribunal were of fact and involved no question of law. Meanwhile, the AO through order dated 26.05.1994 imposed a penalty of Rs. 47,52,648 for understatement of income on sale of cylinders and for bogus claim of depreciation on computers. In first appeal in the penalty proceedings, the CIT(A) by order dated 30.3.1995 confirmed the imposition of penalty. The Tribunal, in second appeal, by order dated 08.04.1996 deleted the penalty as regards sale value of cylinders, and as far as depreciation on computers was concerned, remanded back the matter to the AO with a direction that the assessee be allowed to conduct cross-examination of one Daddan Bhai (the Managing Director of Altos and PCL), and that it (assessee) be also provided with the statement given before the Sales Tax authorities.

3. In penalty proceedings conducted *de novo*, the AO again imposed a penalty of Rs. 47,68,130/- on account of furnishing inaccurate particulars of income in terms of section 271(1)(c) of the Income Tax Act, 1961 (the Act, in short) by making wrong claim for depreciation on computers. The CIT(A) by order 19.12.2001 cancelled the penalty imposed by the AO, which was further upheld by the Tribunal through order dated 20.04.2007, which is in challenge in this appeal.

4. Learned counsel for the revenue, Mr. Sanjeev Rajpal assailed the Tribunal's order on the ground that it ignored the finding in the assessment proceedings that the transactions entered into between the assessee, PCL and Altos for purchase and lease back of computers had been held to be sham and paper transactions. It was urged that the Tribunal erred in holding that complete details had been furnished by the assessee, and therefore there was no concealment. He argued that if the transaction itself is held to be a sham, a mere paper transaction, then the assessee would not be absolved of his liability for concealment and furnishing inaccurate particulars, by merely relying upon the same papers/documents. He further argued that the explanation offered by the assessee to establish ownership and use of the computers was false and *mala fide*, thus attracting Explanation 1 to Section 271 and deeming such amounts in respect of depreciation on computers as concealed income. In this regard, he placed reliance on a decision by a Division Bench of this Court in *Commissioner of Income Tax v. Zoom Communication Pvt. Ltd.*, [2010] 327 ITR 510 (Delhi).

5. Learned counsel for the assessee, on the other hand, defended the impugned judgment. He pointed out that it is a matter of record that the

assessee was not given opportunity to cross-examine Daddan Bhai. It was urged that in penalty proceedings, the assessee is entitled to lead evidence and cross-examine the witnesses; and the failure to enable the assessee to do the same herein, despite directions of the Tribunal through its order dated 08.04.1996 should preclude levy of any penalty, on the assessee. Counsel further urged that the assessee had furnished copies of purchase invoices, details of payments, confirmation from parties (PCL and ALTOS) and details of lease rental, received and offered. The main thrust of his argument was that the mere disallowance of the claim of depreciation was inadequate to attract the levy of penalty; instead, what is needed for attracting penalty under section 271(1)(c) is that inaccurate particulars be actually furnished, which, he claimed, was not the case here, as the assessee had furnished all the relevant details of the transactions between it (the assessee), PCL and ALTOS. To support this argument, counsel placed reliance on *Commissioner of Income Tax v. Reliance Petroproducts Pvt. Ltd.*, 322 ITR 158 (SC) and *Karan Raghav Exports Pvt. Ltd. v. Commissioner of Income Tax*, ITA 1152/2011/Del decided on 14.03.2012.

6. This Court has considered the submissions of the parties. The penalty in dispute in this appeal [imposed by the AO in penalty proceedings conducted *de novo*, cancelled by the CIT(A) which was upheld by the Tribunal] is on account of bogus claim of depreciation amounting to Rs. 37,69,273/- on computers, which as per the AO, were never owned, used or leased by the assessee. It is a matter of record that the assessee purchased 15 computers from PCL, and according to agreement, leased it out to Altos for a period of three years, who took the delivery of the computers on behalf of

the assessee; Altos further sub-leased to PCL. This transaction was ultimately held to be a sham in the assessment proceedings. The CIT(A), in the second round of penalty proceedings, premised its conclusions on the following reasoning while cancelling the penalty levied:

> *"All the documentary evidence filed before the AO and relied upon before me, as per details given in the written submissions filed on 13.7.99, as also reproduced above, have not been disputed by the AO. The Hon'ble Tribunal had confirmed the disallowance of depreciation essentially because it was considered that the transaction was improbable. Even the letter of Shri Dadan Bhai dated 26.3.99, as referred to by the AO in para 8 of the penalty order, indicates that the transaction of purchase of computers by the appellant from M/s. Pertech Computers Ltd. and their leasing to M/s. Altos India Ltd. does not appear to be a sham or paper transaction. The mere fact that the disallowance of depreciation had been confirmed by the Tribunal, does not if so facto, entitle the AO to impose a penalty u/s 271(1)(c). It is also by now a settled proposition of law that the findings in quantum proceedings may be good enough for refusing the assessee's claim of deprecation but were not sufficient for levying penalty for concealment of income as also held by the Hon'ble Tribunal in the assessee's own penalty appeal vide its order dated 8.4.96. this proposition has been upheld by the Hon'ble Supreme Court judgment in 83 ITR 369 and in 123 ITR 458. The prolonged litigation between the appellant and M/s. Altos India Ltd. also goes to support the appellant's case that the computers purchased from M/s. Pertech Computers Ltd. were leased out to M/s. Altos India Ltd. The learned AR's submission and contentions regarding the statement of Shri Dadan Bhai carry weight and deserve to be upheld. Keeping in view te facts and circumstances of the case it is clear that AO has erred in imposing the penalty u/s 271(1)(c) as the same was unwarranted and unjustified."*

7. The Tribunal upheld this reasoning in the following manner:

"The learned CIT(Appeals) has taken into consideration the fact that the assessee had made efforts to recover the computers leased out to Altos which were purchased from PCL. Copy of correspondence between assessee and Altos made are discussed by the learned CIT(Appeals) at pages 35 to 40 of his order and from his correspondence it is seen that the assessee had made efforts to recover the computers leased out to ALTOS. It is further seen that assessee has filed a case for recovery of the computers or to compensate in lieu of returning back the computers. The matter was also listed before one Mr. P.C. Jain, sole Arbitrator and from these facts it is found that the litigation was going on between the assessee and ALTOS. It is further seen that assessee had provided complete details of computers leased out by it after purchasing from PCL. Full particulars of lease rental income were shown by the assessee while filing its return of income were also furnished. Therefore, it cannot be said that assessee has concealed any particular of its income. Of course, assessee made claim of depreciation on account of computer leased out to ALTOS. However, the AO made disallowance of depreciation and the amount of the AO has been confirmed by the Tribunal and on reference the High Court has stated that the finding of the Tribunal are findings of fact. Therefore, they declined to interfere… In the present case, in our considered view, assessee has furnished full particulars relating to the income earned on account of leased out assets as complete details, invoices, agreement etc were filed at every stage. We further note that the AO himself accepted the lease rental income on account o the same computers by passing assessment for A.Y. 1990-91 and 1991-92. The contention of the learned DR that every year is independent and resjudicata does not apply income-tax proceedings, in our considered view, is not well founded, because the assessee has shown lease rental income on the same asses, which were shown in earlier year i.e. 1989-90. Therefore the contention of the learned DR is rejected. Once it is found that the assets have been treated as genuine by the Department, no scope remains for doubting that particulars furnished in earlier year were not correct.

In view of these facts and circumstances, we hold that the learned CIT(Appeals) was justified in canceling the levy of penalty."

8. There is no doubt about the proposition that penalty proceedings are distinct from assessment proceedings, and that a mere addition in the latter does not necessarily attract levy of penalty. To this extent, we, therefore, certainly agree with the assessee's submission. However, the issue does not rest here. Explanation 1 to Section 271 is also relevant, and its intendment, and the implication to the case, if any, will have to be examined. The Explanation reads as:

"Explanation 1.—Where in respect of any facts material to the computation of the total income of any person under this Act,—

(A) such person fails to offer an explanation or offers an explanation which is found by the Assessing Officer or the Commissioner (Appeals) or the Commissioner to be false, or

(B) such person offers an explanation which he is not able to substantiate and fails to prove that such explanation is bona fide and that all the facts relating to the same and material to the computation of his total income have been disclosed by him,

then, the amount added or disallowed in computing the total income of such person as a result thereof shall, for the purposes of clause (c) of this sub-section, be deemed to represent the income in respect of which particulars have been concealed."

9. It cannot be doubted that in order to claim depreciation on the computers, the burden lay upon the assessee to prove its "ownership" and "use". The circular nature of the transactions involving these computers has already been stated above. The following extract from the Tribunal's order dated 22.10.1992 in the assessment proceedings, is relevant for this point:

"So far the question of ownership is concerned, it is necessary to look into the circumstances obtaining in this case, namely, that ALTOS the manufacturer of computers is claimed to have sold the computers to PCL, its selling agent, and PCL in its turn sold the same to the assessee and again the assessee entered into a contract of leasing with M/s. ALTOS... according to the assessee, computers were never taken actual delivery of and they went back form PCL to ALTOS, the computers were sub-leased by it to PCL and according to PACL they were sent to Calcutta and again sub-leased to various parties at Calcutta. Thus, the entire transaction is so inter-woven that it gives a colour of mere payer transaction without any actual transaction of sale. In other words, there is not material to record to establish that the title in computers ever actually passed to the assessee. The assessee had disowned the knowledge of the alleged sublease by ALTOS to PCL and further sub-lease by PACL to various Calcutta parties. The assessee since did not receive delivery of the computers from PCL and allowed it to deliver by PCL to ALTOS, there was implied authority of the assessee with PCL and therefore the assessee cannot get rid of the conduct of his own agent, namely, PCL in dealing with those computers, contrary to the claim of ownership thereof by the assessee. The entire gamut of facts makes it clear that there was no actual delivery of computers to the assessee and the assessee also never cared to know about the whereabouts of those computers... it had nothing to do with the computes except to realize the amount of Rs.25,13,100 from ALTOS which, according to the agreement, the assessee is getting in monthly instalments from ALTOS in all aggregating to Rs.33,42,420 @ Rs.92,845 p.m.

While considering the entire material on record we cannot lose sight of the fact that there is a common Director in ALTOS and PCL, namely Dadan Bhai and as such it was very much convenient for the assessee to deal in the name of two companies with a common man. We fail to understand why a manufacturing concern would take its own manufactured computers on lease and would pay a heavy hiring charges

totaling to Rs.33,42,420 while the computers are valued at a little over Rs.fifty lakhs and that too without getting back the title to the said computers."

10. During hearing before him, the CIT(A) had enquired from the assessee's counsel as to what ultimately happened to the computers, and whether the assessee had claimed ownership of these computers. In response, the assessee filed certain documents based on which it asserted that after expiry of the lease period, it had been trying its level best to get back the computers as leased out, and that it was also pursuing recovery of unrealized lease money. It was stressed that Altos was under liquidation/winding up, and despite prolonged litigation, the assessee had been unable to recover either computers or even unrealized amount of lease money, due to which it suffered great loss.

11. This response given by the assessee, in the opinion of this Court, does not substantiate its claim for treating the tripartite agreements as valid. It is difficult to believe that assessee would not have known the true nature of the transaction, and that it was of the *bona fide* view that it actually "owned" the "leased" computers, on which it claimed depreciation. In this light, the observation of the Supreme Court in *Commissioner Of Income-tax West Bengal Ii v. Durga Prasad More*, [1971] 82 ITR 540 (SC) is relevant that "*the taxing authorities are not required to put blinkers while looking at the documents produced before them' and that 'they are entitled to look into the surrounding circumstances to find out the reality of recitals made in those documents*". Thus, even though the assessee may have furnished all particulars for the tripartite transaction, the fact that what it put up in its return was a sham and mere paper transaction leads us to the inevitable

conclusion that the explanation of the assessee on the question of its ownership and use of the computers is unsubstantiated and *mala fide*. The assessee's response that it attempted to recover the unrealized rental, and the possession of the computers, after the expiry of the lease period of 3 years, does not, by any means, substantiate its explanation or make it *bona fide.* The same is rejected as unacceptable. Therefore, clearly, Explanation 1 to section 271 stands attracted to this case.

12. Consequently, for purposes of section 271(1)(c), the amount of depreciation disallowed is deemed to have been concealed, in respect of which penalty is leviable.

13. The assessee relied on the Supreme Court decision in *Reliance Petroproducts* (supra) where the Court held as follows:

> *"Reading the words in conjunction, they must mean the details supplied in the Return, which are not accurate, not exact or correct, not according to truth or erroneous. We must hasten to add here that in this case, there is no finding that any details supplied by the assessee in its Return were found to be incorrect or erroneous or false. Such not being the case, there would be no question of inviting the penalty under Section* 271(1)(c) *of the Act. A mere making of the claim, which is not sustainable in law, by itself, will not amount to furnishing inaccurate particulars regarding the income of the assessee. Such claim made in the Return cannot amount to the inaccurate particulars.*
>
> *It was tried to be argued that the falsehood in accounts can take either of the two forms; (i) an item of receipt may be suppressed fraudulently; (ii) an item of expenditure may be falsely (or in an exaggerated amount) claimed, and both types attempt to reduce the taxable income and, therefore, both types*

amount to concealment of particulars of one's income as well as furnishing of inaccurate particulars of income. We do not agree, as the assessee had furnished all the details of its expenditure as well as income in its Return, which details, in themselves, were not found to be inaccurate nor could be viewed as the concealment of income on its part. It was up to the authorities to accept its claim in the Return or not. Merely because the assessee had claimed the expenditure, which claim was not accepted or was not acceptable to the Revenue, that by itself would not, in our opinion, attract the penalty under Section 271(1)(c). If we accept the contention of the Revenue then in case of every Return where the claim made is not accepted by Assessing Officer for any reason, the assessee will invite penalty under Section 271(1)(c). That is clearly not the intendment of the Legislature."

There is no doubting the view taken by the Court in *Reliance Petroproducts*, however, the same is of no assistance to the assessee. The distinguishing factor has already been discussed earlier, viz. that the transactions were a sham, and the assessee was could not have been unaware about the same. Furthermore, the revenue, in this connection, relied upon the following extracts from *Zoom Communication* (supra), which are pertinent and applicable to present discussion:

"16. The proposition of law which emerges from this case, when considered in the backdrop of the facts of the case before the Court, is that so long as the assessee has not concealed any material fact or the factual information given by him has not been found to be incorrect, he will not be liable to imposition of penalty under Section 271(1)(c) of the Act, even if the claim made by him is unsustainable in law, provided that he either substantiates the explanation offered by him or the explanation, even if not substantiated, is found to be bonafide. If the explanation is <u>neither substantiated nor shown to be bonafide</u>,

Explanation 1 to Section 271(1)(c) would come in to play and the assessee will be liable to for the prescribed penalty.

19. It is true that mere submitting a claim which is incorrect in law would not amount to giving inaccurate particulars of the income of the assessee, but it cannot be disputed that the claim made by the assessee needs to be bonafide. If the claim besides being incorrect in law is malafide, Explanation 1 to Section 271(1) would come into play and work to the disadvantage of the assessee.

20. The Court cannot overlook the fact that only a small percentage of the Income Tax Returns are picked up for scrutiny. If the assessee makes a claim which is not only incorrect in law but is also wholly without any basis and the explanation furnished by him for making such a claim is not found to be bonafide, it would be difficult to say that he would still not be liable to penalty under Section 271(1)(c) of the Act. If we take the view that a claim which is wholly untenable in law and has absolutely no foundation on which it could be made, the assessee would not be liable to imposition of penalty, even if he was not acting bonafide while making a claim of this nature, that would give a licence to unscrupulous assessees to make wholly untenable and unsustainable claims without there being any basis for making them, in the hope that their return would not be picked up for scrutiny and they would be assessed on the basis of self Assessment under Section 143(1) of the Act and even if their case is selected for scrutiny, they can get away merely by paying the tax, which in any case, was payable by them. The consequence would be that the persons who make claims of this nature, actuated by a malafide intention to evade tax otherwise payable by them would get away without paying the tax legally payable by them, if their cases are not picked up for scrutiny. This would take away the deterrent effect, which these penalty provisions in the Act have."

(emphasis supplied)

14. Having regard to the above discussion, there can be no doubt that the assessee was aware of the true nature of the transaction, despite which the claim for depreciation was made. Its claim was rejected as sham, by this Court – that order has become final. The explanation given by the assessee for the depreciation claim, is neither bonafide, nor substantiated. Therefore, the cancellation of penalty was unwarranted. The impugned order is accordingly set aside; the order of the AO imposing penalty is restored. The appeal is allowed; no costs.

S. RAVINDRA BHAT
(JUDGE)

R.V. EASWAR
(JUDGE)

OCTOBER 19, 2012