

IN THE INCOME TAX APPELLATE TRIBUNAL  
AMRITSAR BENCH, AMRITSAR  
BEFORE SH. SANJAY ARORA, ACCOUNTANT MEMBER

**I.T.A No.474/(Asr)/2017**  
Assessment Year: 2007-08

Mangat Rice and General vs. ITO, Nakodar.  
Mills, Shahkot.

PAN: AABFM 5282B

**(Appellant)**

**(Respondent)**

Appellant by: Sh. Gaurav Dhall, CA

Respondent by: Sh. Charan Das, Sr. DR

Date of hearing : 13.11.2018

Date of pronouncement: 06.12.2018

**ORDER**

Per Sanjay Arora, A.M.

This is an Appeal filed by the Assessee directed against the Order by the Commissioner of Income Tax (Appeals)-2, Jalandhar ('CIT(A)' for short) dated 23.05.2017, dismissing the assessee's appeal contesting its' assessment u/s. 143(3) of the Income Tax Act, 1961 ('the Act' hereinafter) for Assessment Year (A.Y.) 2007-08 vide order dated 14.12.2009.

2. The principal issue arising in the instant appeal is the maintainability in law, and in the facts and circumstances of the case, of an addition for Rs.4.39 lacs sustained by the first appellate authority. The background facts are that the assessee, a partnership firm in the business of rice milling, filed its' return of income for the year on 18.03.2008 declaring 'Nil' income. It's trade debtors and trade creditors, reflected at Rs.9.42 lacs and Rs.32.18 lacs respectively as at the year-end, i.e., 31.03.2007, per its final accounts, were sought to be verified by the

Assessing Officer (AO) by calling information there-from u/s.133(6) of the Act. The dispute under reference pertains to two creditors, as under:

- (a) Jai Ram Jagdish Chandra, Mehatpur (JRJC) : Rs.6,03,837.83
- (b) Sohan Singh Satpal, Mehatpur (SSS) : Rs.8,38,871.58

The copy of the assessee's account in the books of JRJC showed a sum of Rs.9,03,837.83 as due from the assessee, which was duly recovered during financial year (f.y.) 2004-05 (Rs.4 lacs) and f.y. 2005-06 (Rs.5.04 lacs), fully liquidating the debt. The entire amount was received in cash, not exceeding Rs.20,000/- per day. This position was confirmed per deposition on oath u/s.131 of the Act by Shri Jagdish Chander, proprietor, on 15.07.2009. The assessee's accounts revealed payment of Rs.3 lacs during f.y. 2003-04, reducing the creditors' balance from Rs.9.04 lacs to Rs.6.04 lacs as on 31.03.2004, whereafter no payment was made. The payment recorded in the assessee's books was again in cash, at Rs.20,000/- per day. Similarly, copy of the assessee's account in the books of SSS recorded the assessee to be a trade debtor for Rs.8.39 lacs as on 01.04.2005, which was received during f.y. 2005-06 (Rs.4 lacs) and the balance (Rs.4.39 lacs) during f.y. 2006-07, i.e., the relevant previous year. The entire payment received was, again, in cash, not exceeding Rs.20,000/- per day. This state of affairs was confirmed by Shri Gurcharan Singh s/o Smt. Gurdeep Kaur, proprietor, u/s.131 of the Act dated 15.07.2009. The copies of the account statements as well as the statements u/s.131 were supplied to the assessee, who denied having made any payments, i.e. except as recorded in its' books of account. Shri Prem Kumar, its' managing partner, had in fact been declared a proclaimed offender (PO) on 15.09.2004 in criminal proceedings filed against him by Markfed, a PSU, whose paddy was being milled by the assessee-firm. It was inconceivable that a person who had gone in hiding would surface every other day to pay cash to these firms at Rs.20,000/-, i.e., discharging a time barred debt. The assessee-firm was in fact

facing a financial crisis, and had no funds or, in fact, source of income. Additions were made for the amount outstanding in the assessee's books. The matter traveled to the Tribunal which, vide its order dated 30.12.2017 (in ITA No.616/Asr/2013 copy on record), set aside the matter to the file of the first appellate authority for a decision *de novo* per a speaking order after providing adequate opportunity of hearing to the assessee. The Id. CIT(A) has, in the second round, confirmed the additions for the current year to the extent of the payment recorded as received by the creditor-firm, i.e., at Rs.4,38,872/- (in the case of SSS). For the other amounts, directions were issued by him u/s. 150(1) of the Act to, similarly, bring the amounts as paid by the assessee during those years, i.e., as per the books of the creditors, to tax.

3. I have heard the parties and perused the material on record and given a careful consideration to the matter.

The assessee's case is that no payment not recorded in its' books of account has been made by it, and which has been recorded on their own by the two creditors. Considering the amount as no longer receivable (from the assessee), it is claimed that they, to protect the erosion of their capital, had booked their own money as cash received from the assessee. That is, the entries of cash received from the assessee in their accounts are false, and no adverse consequence on that basis should follow. On being questioned by the Bench that, assuming so, so that section 69A may not apply, how would section 41(1), also invoked by the Revenue, not become applicable inasmuch as the creditors have denied any debt as due to them by the assessee as on 31.03.2007. The Id. counsel, Shri Dhall, would submit that section 41(1) would not apply as the assessee still admits its' liability, to the extent stated, to the named creditors. The same finding reflection in the assessee's books of account from year to year, for which he would refer to the balance-sheets for the later years, enclosed as part of the paper-book (PB), the

same amounts to an admission of liability, so that the limitation for legal recovery thereof would also not apply. The Revenue's case, on the other hand, is that the entries in the books of the creditors are backed by their statements u/s.131, which are admissible in evidence. Further, why would a creditor show receipt of money from a debtor without actually receiving it, jeopardizing his recovery, if any, in future? Why, he would rather claim the bad debt as a tax deductible expenditure. There is thus no merit in the assessee's stating of having not paid any money to the creditors. It is not unusual for a debtor to arrive at a compromise with a creditor and pay in installments over a period of time, i.e., in time of financial difficulty, as indeed the assessee admittedly has with JRJC in the past. Besides, the payment could also be prompted by consideration of safeguarding its' reputation in the market; the assessee having been already embroiled in a dispute with a government agency. The payments may not necessarily have been made in installments of Rs. 20,000/-, which is so booked only to eschew non-deduction as business expenditure u/s. 40A(3/3A). In any case of the matter, denial of the assessee's liability thereto by the creditors would attract section 41(1) inasmuch as the liability stands extinguished, i.e., ceases to exist. Its' reflection in the assessee's account, which perhaps continues to date, would be of little consequence inasmuch as, in effect and substance, it does not represent an actual liability to a trade creditor/s.

My first observation in the matter, and even as observed during hearing, is that even assuming that the creditors have not been paid by the assessee, their denial of the assessee's impugned liability to them, would amount to a remission of a trade liability, attracting section 41(1) of the Act, which reads as under:

**Profits chargeable to tax.**

**41.** (1) Where an allowance or deduction has been made in the assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee (hereinafter referred to as the first-mentioned person) and subsequently during any previous year,—

(a) the first-mentioned person has obtained, whether in cash or in any other manner whatsoever, any amount in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cessation thereof, the amount obtained by such person or the value of benefit accruing to him shall be deemed to be profits and gains of business or profession and accordingly chargeable to income-tax as the income of the previous year, whether the business or profession in respect of which the allowance or deduction has been made is in existence in that year or not; or

(b) the successor in business has obtained,...

*Explanation 1.*—For the purposes of this sub-section, the expression “loss or expenditure or some benefit in respect of any such trading liability by way of remission or cessation thereof” shall include the remission or cessation of any liability by a unilateral act by the first mentioned person under clause (a) or the successor in business under clause (b) of that sub-section by way of writing off such liability in his accounts.

The assessee stating that it is liable to the creditors to the stated extent, as borne out by its’ audited accounts, would amount to naught in view of their stating on oath – which has evidentiary value, of having received their dues from the assessee over a period of time, which is in agreement with their books of account. The said statements have not been rebutted in any manner, as through cross examination or in any other manner. *That is, either way, the assessee cannot succeed.* It would be a different matter where the decision rested only upon a finding as to whether, in the given facts and circumstances of the case, the assessee can be said to have paid or, as the case may be, not paid the two trade creditors under reference, and which would require the tribunal to examine closely the facts, sifting that proved from that unproved, to arrive at a finding of fact, which may, at any rate, be issued based on a preponderance of probabilities. It could be, as claimed – the assessee being unable to pay, that the parties, with a view to introduce their undisclosed income/wealth without tax, routed the same as cash received from the assessee. The same in fact is a serious charge, i.e., of the two creditors being tax evaders, which cannot be made without a firm basis, at least one of which a court could take judicial notice. That apart, it involves assumptions, for which there is no basis, so that it would only be presumptuous. In fact, no tax advantage arises as they could have,

equivalently, claimed the entire amount as a bad debt while introducing their income/funds, assuming so, as income, so that there is not net tax liability. The claim of bad debts in accounts, based as it is on the best judgment of the management, does not prejudice the creditors' right to recover through persuasion or recourse to the legal process. The limitation, even as stated by Shri Dhall, runs from the last acknowledgement of the debt, so that the debts were not barred by time during the period the payment is stated to have been received from the assessee, who admittedly has not paid the creditors even to date. To, though, no explanation or reason for non-payment, even as the balance-sheets for the subsequent years reflect business. Such a payment would, while proving its' liability thereto as existing, only be to the benefit of the creditors, even if constituting their income liable to tax. We could go on further. However, it is not necessary to dwell further in the matter; even the foregoing discussion being made only to emphasize that a decision as to payment – a matter of fact, also, on balance, cannot be said to be skewed in favour of the assessee, even as there is substance in the assessee's version of being unable to pay in view of the precarious situation, though non-reflection of cash in its accounts, by itself, may not be conclusive of the matter, as also observed by the tribunal in the first round. This is as even considering non-payment, as afore-stated, the creditor/s claiming to have received the payment, the same ceases to exist; the assessee being not longer liable to pay the same. The assessee has, without doubt, benefited from it being no longer liable in respect of a trade liability, deduction *qua* which stands claimed and allowed in an earlier year in computing business income, so that it stands to gain to that extent. The same would stand to be regarded as business income, or a benefit or advantage, of commercial nature, arising from and in the course of business, i.e., on first principles, so as to regarded as business income, even if it were not to be codified u/s.41(1) reproduced supra (refer: *CIT v. T.V. Sundaram Iyengar & Sons*

*Ltd.* [1996] 222 ITR 344 (SC)) Even if, therefore, agreeing with the assessee, that it did not pay the creditors, who were therefore paid by someone else, whoever it might be, the assessee stands to gain to that extent *qua* a trade liability arising in the course of its' business. Rather, it is only as the same is not paid by the assessee that it benefits from the cessation/ remission of liability, and s. 41(1) gets attracted.

To put succinctly, in each of the three scenarios the assessee is liable to be assessed for the amount stated as received by the creditors during a particular year. If the assessee paid the creditors, s. 69A would come into play. If, on the other hand, someone paid them on assessee's behalf, s. 41(1) would get attracted on account of cessation of a trade liability; the assessee admittedly not incurring any other liability in lieu of such payment. Thirdly, if, as claimed, no amount stands paid to the creditors – with they introducing their own money, s. 41(1) would again get attracted on account of remission of the trade liability. I, therefore, have no hesitation in upholding the assessment of Rs.4,38,872/- as the assessee's income, being the amount by which the assessee's liability to SSS has undergone reduction during the current year. Though one could argue that the assessee's accounts reflecting a total liability to the trade creditors at Rs.14.43 lacs, which does not exist as at the year-end, so that the entire amount ought to be, as by the AO, assessed as income, it needs to be appreciated, that the evidence with the Revenue, in the form of denial of the assessee's debt in their favour by the trade creditors, itself states of reduction in the said liability over a period of time. Accordingly, I agree with the Id. CIT(A) that the reduction obtaining during a particular year is to be assessed as income for that year. His directions, accordingly, to that effect to the AO u/s. 150(1), subject to the fulfillment of the conditions u/s. 150(2), cannot be faulted. However, of the payment of Rs. 4 lacs to JRJC during f.y. 2004-05, Rs.3 lacs stands already paid during f.y. 2003-04 as per the assessee's accounts. Accordingly, it is only the difference, i.e., Rs.1.0 lac, that can be assessed as

income u/s. 41(1) for AY 2005-06 on that account. This aspect shall be duly considered by the AO while giving effect to the said directions by the Id. CIT(A). Apart there-from, I, therefore, find no reason to interfere with his findings. I decide accordingly.

4. In the result, the assessee's appeal is disposed of on the terms aforesaid.

*Order pronounced in the open Court on December 06, 2018*

Sd/-  
(Sanjay Arora)  
Accountant Member

Date: 06.12.2018

*PKK*

Copy of the order forwarded to:

- (1) The Assessee
- (2) The ITO concerned
- (3) The CIT(A)
- (4) The CIT concerned
- (5) The Sr.D.R., I.T.A.T.

True copy

By Order