

**IN THE INCOME TAX APPELLATE TRIBUNAL
“D” BENCH MUMBAI**

**BEFORE SHRI SAKTIJIT DEY, VICE PRESIDENT &
SHRI MAKARAND VASANT MAHADEOKAR, ACCOUNTANT MEMBER**

**ITA No. 7726/Mum/2025
(Assessment Year: 2018-19)**

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| MKF International 1903/1905, Aarus Wing, Wallace Fortuna, Shivdas Chapsi Marg, Opp-Fazlani School, Chinchbunder HO, Mumbai-400 009 | Vs. | DCIT Circle 17(1), Kautilya Bhavan, BKC, Mumbai – 400 051 |
| PAN/GIR No. ABHFM5244N | | |
| (Applicant) | | (Respondent) |

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| Assessee by | Shri Dharmesh Shah a/w Ms. Mitali Parekh, Ld. ARs |
| Revenue by | Shri Umashankar Prasad, Ld. DR |

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| Date of Hearing | 10.02.2026 |
| Date of Pronouncement | 12.02.2026 |

आदेश / ORDER

PER MAKARAND VASANT MAHADEOKAR, AM:

This appeal is preferred by the assessee against the order dated 04.11.2025 passed by the Commissioner of Income Tax (Appeals), National Faceless Appeal Centre, Delhi [hereinafter referred to as “CIT(A)”] under section 250 of the Income Tax Act, 1961[hereinafter referred to as “the Act”], arising out of the

assessment order dated 30.09.2021 passed by the Income Tax Officer, Ward 7(2)(1), Mumbai[hereinafter referred to as “Assessing Officer”] under section 143(3) of the Act for Assessment Year 2018–19.

Facts of the Case

2. The assessee is a partnership firm. It filed its return of income on 25.06.2018 declaring total income at Nil. The return was processed under section 143(1). Subsequently, the case was selected for complete scrutiny. As recorded in the assessment order, the reasons for selection of scrutiny were Investment in immovable property and Share capital / Other capital. The Assessing Officer noted that the assessee commenced business on 15.12.2017, the year under consideration being the first year of business. During the year, the assessee entered into an agreement dated 17.01.2018 for transfer of tenancy of a shop situated at the ground floor of Liberty Cinema building. During the year, the assessee introduced capital aggregating to Rs. 19,06,08,525/-.

3. The Assessing Officer issued notice under section 142(1) calling for Computation of income, Audit report, Bank statements, Partnership deed, Confirmation of capital introduced with supporting documents, Fund flow statement and Source and proof of investment in property. The assessee sought adjournments and did not furnish complete details in response to earlier notices. A show cause notice dated 28.09.2021 was issued

proposing addition under section 68 in respect of capital introduced.

4. In response to the show cause notice, the assessee furnished the details and submitted that the capital was introduced by four partners out of which three partners were Non-Residents. It was also submitted that the funds represented business income earned outside India, particularly in UAE and the transactions were effected through proper banking channels and reflected in the partners' bank accounts.

5. The Assessing Officer held that the assessee failed to establish the nature and source of capital introduced with supporting documentary evidence. Accordingly, the Assessing Officer treated the capital introduced of Rs. 19,06,08,525/- as unexplained cash credit under section 68 and brought the same to tax at the special rate under section 115BBE. Penalty proceedings under section 270A were also initiated.

6. Aggrieved, the assessee preferred appeal before the CIT(A). Before CIT(A), the assessee reiterated that capital was introduced by partners through banking channels, funds represented income earned outside India, identity of partners stood established and remittances were reflected in bank accounts. The assessee also filed additional evidences before the CIT(A).

7. The CIT(A) upheld the action of the Assessing Officer, observing that the assessee failed to substantiate the nature and source of capital introduced. It was also observed that no proper

documentary evidence establishing source of foreign remittances was furnished. The CIT(A) also noted that the remand report concurred with the Assessing Officer's findings and additional evidences were rejected for violation of Rule 46A.

8. Aggrieved by the order of the CIT(A) the assessee is in appeal before us raising following grounds of appeal:

1. *The Ld. CIT(A) NFAC has erred in law and in facts in upholding the addition u/s 68 of the Act amounting to Rs. 19.06.08.525/- in respect of the capital contribution made by all the partners.*
2. *The appellant craves leave to add, amend, alter, delete all or any of the forgoing grounds of appeal.*

The assessee also fined additional grounds of appeal which are:

1. *The Ld. CIT (A) ought to have appreciated that the notice issued u/s. 143(2) of the Act is invalid and deserves to be quashed. Hence, the consequential assessment order is also void ab initio.*
2. *The Ld. CIT (A) ought to have appreciated that the assessment order passed u/s. 143(3) of the Act is invalid and without jurisdiction.*

9. During the course of hearing, the learned Authorised Representative (AR) submitted that the Assessing Officer has, in substance, required the assessee to explain the source of the source of capital introduced by the partners, particularly the Non-Resident partners. It was contended that once the identity of the partners and the fact of introduction of capital through banking channels stood established, the Assessing Officer could not insist upon the assessee firm to further prove the source of funds in the hands of the partners beyond the primary evidences furnished.

10. The learned AR further submitted that before the CIT(A), the assessee had furnished additional documentary evidences substantiating the capital introduced. However, the CIT(A) rejected the additional evidences on the basis of the remand report obtained from the Assessing Officer. It was specifically contended that no copy of the remand report was furnished to the assessee for rebuttal and, therefore, the assessee was deprived of an effective opportunity to meet the observations made therein. It was submitted that such action is in violation of the principles of natural justice.

11. The learned AR invited attention to the documents placed in the paper book and submitted that the material placed on record sufficiently explains the source of capital introduced by the partners. Reference was made to the following documents:

- i. Financial statements of the partners placed at page Nos. 52 to 54 of the paper book.
- ii. Relevant extracts of bank statements of the assessee evidencing receipt of funds from Non-Resident partners placed at page Nos. 74 to 76 of the paper book.
- iii. Residency certificates of the Non-Resident partners placed at page Nos. 77 to 79 of the paper book.
- iv. Affidavits from the partners confirming the capital introduced in the firm placed at page Nos. 80 to 84 of the paper book.

It was submitted that the identity of the partners, their residential status, the fact of remittance through banking

channels and confirmation of capital contribution stand duly evidenced by the aforesaid documents.

12. The learned Authorised Representative further placed reliance upon the judgment of the Hon'ble Gujarat High Court in ***Darshan Enterprise v. ACIT*** reported in **(2022) 441 ITR 473**, which has been followed by the Co-ordinate Bench in **ITA No. 7752/DEL/2019 in the case of Gazal Caterers**. The learned AR also placed reliance upon the judgment of the Hon'ble High Court of Telangana in **Nova Medicare v. Income-tax Officer** reported in **[2023] 459 ITR 477**.

13. Per contra, the learned Departmental Representative (DR) supported the orders of the Assessing Officer as well as the CIT(A) and submitted that the assessee has failed to satisfactorily discharge the onus cast upon it under section 68 of the Act. The learned DR contended that although the assessee has produced copies of bank statements and confirmations of the Non-Resident partners, the real source of funds credited in the foreign bank account has not been explained. It was submitted that the explanation furnished by the assessee merely shows routing of funds through banking channels, but does not establish the origin of such funds. The learned DR invited our attention to the bank statement of the Non-Resident partners maintained with Emirates NBD Bank, which is stated to be a joint account held by all the partners. It was pointed out that the said bank account reflected an opening balance of AED 11,610,100. The learned Departmental Representative further drew attention to a specific

entry dated 31.12.2017 showing cash deposit of AED 1,000,000 in the said bank account. It was submitted that the assessee has not explained the nature and source of the said opening balance nor the source of the cash deposit of AED 1,000,000. According to the learned DR, in absence of explanation regarding the source of funds credited in the foreign bank account, the creditworthiness of the partners remains unproved. It was thus contended that the assessee has failed to satisfactorily establish the financial capacity of the partners to introduce capital in the firm.

14. The learned DR further invited our attention to paragraph 14 of the judgment of the Hon'ble Gujarat High Court in **Darshan Enterprise v. ACIT (supra)**, which has been relied upon by the learned AR. The relevant extract relied upon by the learned Departmental Representative reads as under:

“When a partnership firm says that it received a particular amount in its capital through its partners and the identity of such partners with necessary details is disclosed, any further information in that regard would be asking the assessee to disclose source of the source. Even this part has been taken care of by the firm. In other words, the source of the source has also been disclosed.”

15. The learned DR submitted that the reliance placed by the assessee on the above decision is misplaced. According to him, the distinguishing feature in the case before the Hon'ble High Court was that the firm had not only established the identity of the partners and genuineness of the transaction, but had also explained the source of funds in the hands of the partners.

Therefore, the Hon'ble High Court observed that even the source of source had been disclosed. In the present case, however, it was contended that the assessee has failed to explain the source of funds reflected in the foreign bank account of the Non-Resident partners.

16. The learned DR further submitted that certain additional evidences were admittedly filed before the CIT(A), which were not part of the assessment record. It was contended that the CIT(A) rejected such additional evidences on the basis of the remand report obtained from the Assessing Officer. However, it was fairly submitted that in the event this Bench is inclined to consider such additional evidences, and particularly in view of the grievance raised by the assessee regarding non-supply of the remand report for rebuttal, the matter may appropriately be restored to the file of the Assessing Officer for proper verification.

17. We have carefully considered the rival submissions, perused the orders of the authorities below and examined the material placed on record including the judicial precedents relied upon by both the parties.

18. The principal issue that arises for our adjudication is whether the addition of Rs. 19,06,08,525/- made under section 68 of the Act on account of capital introduced by the partners in the assessee-firm can be sustained in law.

19. Section 68 of the Act reads as under:

68. Where any sum is found credited in the books of an assessee maintained for any previous year, and the assessee offers no explanation about the nature and source thereof or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the sum so credited may be charged to income-tax as the income of the assessee of that previous year :

Provided that where the sum so credited consists of loan or borrowing or any such amount, by whatever name called, any explanation offered by such assessee shall be deemed to be not satisfactory, unless,—

- (a) the person in whose name such credit is recorded in the books of such assessee also offers an explanation about the nature and source of such sum so credited; and*
- (b) such explanation in the opinion of the Assessing Officer aforesaid has been found to be satisfactory:*

Provided further that where the assessee is a company (not being a company in which the public are substantially interested), and the sum so credited consists of share application money, share capital, share premium or any such amount by whatever name called, any explanation offered by such assessee-company shall be deemed to be not satisfactory, unless—

- (a) the person, being a resident in whose name such credit is recorded in the books of such company also offers an explanation about the nature and source of such sum so credited; and*
- (b) such explanation in the opinion of the Assessing Officer aforesaid has been found to be satisfactory:*

Provided also that nothing contained in the first proviso or second proviso shall apply if the person, in whose name the sum referred to therein is recorded, is a venture capital fund or a venture capital company as referred to in clause (23FB) of section 10.

20. Judicial interpretation has consistently held that the initial burden cast upon the assessee under section 68 is to establish Identity of the creditor, Genuineness of the transaction and Creditworthiness of the creditor. The issue in the present case is

whether, in respect of capital contribution by partners, the firm is further obliged to establish the source of funds in the hands of the partners, failing which the credit can be treated as income of the firm.

21. The first proviso to section 68 provides that where the sum so credited consists of loan or borrowing or any such amount, the explanation offered by the assessee shall be deemed to be not satisfactory unless (a) the person in whose name such credit is recorded also offers an explanation about the nature and source of such sum; and (b) such explanation is found satisfactory by the Assessing Officer.

22. Capital contribution by a partner stands on a distinct legal footing. It is neither a loan nor a borrowing. It represents ownership interest in the firm and forms the substratum of the business. The relationship between the firm and partner in respect of capital is not that of debtor and creditor in the ordinary commercial sense.

23. Even otherwise, the first proviso merely requires that the person in whose name the credit is recorded must also offer an explanation regarding the nature and source of such sum and such explanation must be found satisfactory. In the present case the partners have filed affidavits confirming the capital contribution. Residency certificates of the Non-Resident partners are on record. Financial statements of the partners are on record. Bank statements evidencing remittance through banking

channels are on record. Thus, the persons in whose names the credits are recorded have owned the contributions and offered explanation.

24. The learned DR has doubted the source of funds in the foreign bank account of the partners, referring to opening balance and a cash deposit. Such enquiry, in our considered view, pertains to the financial affairs of the partners and not to the firm. If the Revenue is not satisfied with the explanation of the partners regarding their source of funds, appropriate proceedings may be undertaken in their individual assessments in accordance with law. Section 68 does not authorise the Assessing Officer to treat capital contribution as income of the firm merely because he entertains doubts about the ultimate source in the hands of the partner.

25. The Hon'ble High Court of Telangana in *Nova Medicare v. Income-tax Officer* (459 ITR 477) has observed:

14. After thorough consideration of all relevant aspects, we are of the view that issue raised in this appeal is squarely covered by the decision of this Court in M. Venkateswara Rao (supra) which is binding on us. That was also a case where certain cash credits were advanced by the partners, which according to the revenue authorities remained unexplained and accordingly were added to the income of the firm. In the facts of that case, this Court held as follows:

7. It is a matter of record that the respondent-firm comprises of ten partners and each of them made contributions, be it in the form of cash or bank guarantees to be furnished to the Government, at the commencement of business. The returns submitted by the respondent-firm were processed, and the facts and figures furnished by it were accepted. However, the matter

was reopened at a later point of time. The Assessing Officer treated the capital raised by the firm in the form of contributions made by the partners as income. This conclusion was arrived at on the ground that source of income for the partners was not explained. Learned counsel for the appellant placed reliance upon the judgment of the Patna High Court in *CIT v. Anupam Udyog* [1983] 142 ITR 133/15 Taxman 259. The Tribunal rested its conclusions upon the judgment of the Bombay High Court in *Narayandas Kedarnath v. CIT* [1952] 22 ITR 18 and that of Allahabad High Court in *CIT v. Jaiswal Motor Finance* [1983] 141 ITR 706.

8. Section 68 of the Act no doubt directs that if an assessee fails to explain the nature and source of credit entered in the books of account of any previous year, the same can be treated as income. In this case, the amount, that is sought to be treated as income of the firm, is the contribution made by the partners, to the capital. In a way, the amount so contributed constitutes the very substratum for the business of the firm. It is difficult to treat the pooling of such capital, as credit. It is only when the entries are made during the course of business that can be subjected to scrutiny under section 68 of the Act.

9. Even otherwise, it is evident that the respondent explained the amount of Rs. 76,57,263 as the contribution from its partners. That must result in a situation, where Section 68 of the Act can no longer be pressed into service. However, in the name of causing verification under section 68 of the Act, the Assessing Officer has proceeded to identify the source for the respective partners, to make that contribution. Such an enquiry can, at the most be conducted against the individual partners. If the partner is an assessee, the concerned Assessing Officer can require him to explain the source of the money contributed by him to the firm. If on the other hand, the partner is not an assessee, he can be required to file a return and explain the source. Undertaking of such an exercise, vis-a-vis the partnership firm itself, is impermissible in law. In the judgment relied upon by the appellant itself, the Patna High court held asunder (page 137 of 142 ITR):

"If there are cash credits in the books of a firm in the accounts of the individual partners and it is found as a fact that cash was received by the firm from its partners, then in the absence of any material to indicate that they are the profits of the firm, they cannot be assessed in the hands of the firm, though they may be assessed in the hands of the individual partners. Cash credits in the individual accounts of members of a joint family with third party cannot be assessed as the income of the family unless the Department is charges the burden of proof to the contrary."

10. Therefore, the view taken by the Assessing Officer that the partnership firm must explain the source of income for the partners regarding the amount contributed by them towards capital of the firm cannot be sustained in law.

11. As regards the other amount i.e., unexplained credit entries, the Tribunal took the view that the amount represented the security deposits made by the retail dealers, and the source thereof was properly explained. Nowhere in the order of assessment, the Assessing Officer recorded any finding to the effect that he verified the matter from the respective retail dealers and that such dealers have denied of making deposits. In the field of Arrack business, it is not uncommon that the retail dealers are required to keep security deposits with the supplier. At any rate, it is a pure question of fact.

12. Therefore, the appeal is dismissed.

15. Following and applying the aforesaid decision of this Court, Patna High Court in Anurag Rice Mills (supra) held that in such circumstances the unexplained cash credits would have to be assessed at the hands of the partners of the firm and not the firm itself. Such amounts could not have been treated as income of the firm by relying upon section 68 of the Act.

26. Similarly, the Hon'ble Gujarat High Court in Darshan Enterprise v. ACIT (441 ITR 473) held:

17. Once it is established that the amount has been invested by a particular person, be he a partner or an individual, then the responsibility of the assessee-firm is over. The assessee-firm cannot ask

that person who makes investment where the money invested is properly taxed or not. The assessee is only to explain that this investment has been made by the particular individual and it is the responsibility of that individual to account for the investment made by him. If that person owns that entry, then the burden of the assessee-firm is discharged. It is open to the Assessing Officer to undertake further investigation with regard to that individual who has deposited this amount. So far as the responsibility of the assessee-firm is concerned, it is satisfactorily discharged. Whether that individual person is an income tax payer or not or from where he has brought this money is not the responsibility of the firm. The moment the firm gives a satisfactory explanation and produces the person who has deposited the amount, then the burden of the firm is discharged and in that case that credit entry cannot be treated to be the income of the firm for the purposes of income tax. It is open to the Assessing Officer to take appropriate action under Section 69 of the Act against the person who has not been able to explain the investment.

26. A harmonious reading of section 68 and its provisos leads to the conclusions that the Legislature has consciously imposed an additional burden in respect of closely held companies receiving share capital. No such legislative mandate has been imposed in respect of partnership firms receiving capital from partners. Judicial precedents consistently hold that capital introduced by partners cannot be assessed in the hands of the firm once identity and ownership are established. Enquiry into the source of funds in the hands of the partner is permissible only in the assessment of the partner. To interpret section 68 in a manner that compels a partnership firm to prove the “source of source” in the hands of partners would amount to judicially extending the scope of the proviso beyond the legislative intent.

27. We also deem it appropriate to deal with the procedural aspect relating to the remand report and the request of the

learned DR for restoration of the matter to the file of the Assessing Officer. It is an admitted position on record that additional evidences were furnished by the assessee before the CIT(A). A remand report was called for from the Assessing Officer. However, the additional evidences were rejected by the CIT(A). The remand report was neither accepted in favour of the assessee nor properly confronted to the assessee for rebuttal. The assessee has specifically contended that a copy of the remand report was not furnished to it before being relied upon. It is a settled principle of natural justice that any material sought to be used against an assessee must be supplied and an opportunity must be afforded to rebut the same. Reliance upon a remand report without furnishing the same to the assessee vitiates the appellate process.

28. However, even assuming that there was procedural irregularity at the stage of the CIT(A), the crucial question before us is whether remand of the matter to the Assessing Officer is warranted. The learned DR has submitted that in view of the additional evidences and the doubts regarding the foreign bank account, the matter may be restored to the Assessing Officer for fresh verification. We are unable to accept this contention for the following reasons:

- i. First, the addition under section 68 has been made in the hands of the firm in respect of capital introduced by partners. As discussed in detail hereinabove, the legal position is well settled that once the identity of the partners and the fact of capital contribution are established, the addition cannot be sustained in the hands of the firm. Any

further enquiry into the source of funds in the hands of the partners must be undertaken in their individual assessments. When the addition itself is legally unsustainable in the hands of the firm, remanding the matter for further factual verification would be an empty formality and would amount to prolonging litigation without legal basis.

- ii. Second, the assessment year under consideration is the first year of operations of the assessee-firm. The firm commenced business during the relevant previous year. There is no material on record to suggest that the firm had generated undisclosed profits which were rerouted through the partners in the guise of capital contribution. In absence of any such allegation or finding, the hypothesis that the firm's own undisclosed income has been introduced through partners does not arise.
- iii. Third, the Revenue has not brought any material on record to demonstrate that the partners are fictitious or that the capital introduced in fact belonged to the firm. The entire case of the Revenue rests on suspicion regarding the foreign bank account entries of the partners. Such suspicion cannot confer jurisdiction to tax the amount in the hands of the firm contrary to settled legal principles.
- iv. Fourth, the purpose of remand is to cure a factual deficiency where adjudication depends upon factual verification. In the present case, the issue is primarily legal, namely, whether capital introduced by partners can be assessed in the hands of the firm under section 68 in the absence of any material indicating that the amount represents income of the firm. That issue stands concluded in favour of the assessee by binding judicial precedents.

29. Therefore, even though there may have been procedural lapses at the stage of the CIT(A) in dealing with the remand report, we are of the considered view that remanding the matter back to the Assessing Officer would serve no useful purpose, as

the addition itself is not legally sustainable in the hands of the firm. Accordingly, the request of the learned DR for restoration of the matter to the file of the Assessing Officer is rejected.

30. In view of the foregoing discussion, we reiterate that the addition made under section 68 in the hands of the assessee-firm cannot be sustained and is directed to be deleted.

31. At the time of hearing, the learned Authorised Representative did not press the additional grounds of appeal challenging the validity of notice issued under section 143(2) and the jurisdiction of the assessment framed under section 143(3) of the Act.

32. In view of the statement made at the Bar, the additional grounds are dismissed as not pressed and are, therefore, not adjudicated.

33. In the result, the appeal of the assessee is allowed.

Order pronounced in the open court on 12.02.2026.

Sd/-
(SAKTIJIT DEY)
VICE PRESIDENT

Sd/-
(MAKARAND VASANT MAHADEOKAR)
ACCOUNTANT MEMBER

Mumbai, Dated 12/02/2026
Dhananjay, Sr.PS

आदेश की प्रतिलिपि अग्रेषित / Copy of the Order forwarded to :

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent.
3. संबंधित आयकर आयुक्त / The CIT(A)
4. आयकर आयुक्त (अपील) / Concerned CIT

5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, मुम्बई / DR, ITAT, Mumbai
6. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER,

सत्यापित प्रति //True Copy//

1.

उप/सहायक पंजीकार (Asst. Registrar)
आयकर अपीलीय अधिकरण, मुम्बई/ ITAT, Mumbai