

IN THE INCOME TAX APPELLATE TRIBUNAL  
“A” BENCH : BANGALORE

BEFORE SHRI N.V. VASUDEVAN, JUDICIAL MEMBER  
AND SHRI ABRAHAM P. GEORGE, ACCOUNTANT MEMBER

ITA No. 626/Bang/2015
Assessment year : 2010-11

The Deputy Commissioner of Income Tax, Circle 1, Udupi.	Vs.	M/s. Mahalasa Exports, S.No.75-1 A 3B, Rajaji Road, Hiriadka, Udupi – 576 113. <b>PAN : AAEFM 4143Q</b>
APPELLANT		RESPONDENT

Appellant by	:	Shri Chandrashekar, Advocate
Respondent by	:	Smt. Nandini Das, Jt. CIT(DR)

Date of hearing	:	04.08.2015
Date of Pronouncement	:	14.08.2015

**ORDER**

*Per N.V. Vasudevan, Judicial Member*

This appeal by the Revenue is against the order dated 2.1.2015 of the CIT(Appeals), Mangalore relating to assessment year 2010-11.

2. In this appeal, the Revenue has challenged the order of CIT(Appeals) cancelling the order of Assessing Officer imposing penalty on the assessee u/s. 271(1)(c) of the Act.

3. The facts and circumstances under which penalty was imposed on the assessee by the AO are as follows. The assessee is a partnership firm in the business of export of cashew kernels after processing the cashew nuts. There was a survey at the business premises of the assessee, During the course of survey, excess cash of Rs.4,05,124/- and deficit stock of cashew kernels of 10,438 kgs was found. The assessee failed to explain these discrepancies at the time of survey. It was also noticed by the Assessing Officer that the gross profit declared by the Assessee was at 5.37% and net profit 2.2% which in his opinion was very low as compared to other cashew manufacturers placed similarly as that of the assessee. According to the AO in comparable cases, the yield of cashew kernels outturn was in the range of 22% - 23% as against 19.85% shown by the assessee. When pointed out, the assessee vehemently argued that the results shown were genuine.

4. The AO observed that though the assessee has maintained regular books of accounts and supporting documents, considering the wide variation in the gross profit and yield as compared to other units placed similarly, the AO proposed to assess the income by adopting yield at 22%.

5. Regarding the excess cash, it was submitted by the assessee that the same was due to the omission to record cash sales of Rs.3,81,910/- of low grade rejected cashew kernel. Regarding the difference of 10,438 kgs. shortage of stock, it was also explained that the same is due to non-recording of the above sold amount of 9,050 kgs of cashew rejections at Rs.3,81,910

6. Regarding low out-turn and profit ratios, it was argued by the Assessee that the same are out of their control. Cashew being volatile market, not everybody gets similar profits. Though for the F.Y.2009-10 the GP was low, for the FY 2011-12 the results were comparatively very good which goes to show that the Assessee does not manipulate the results. The Assessee also explained that during the previous year, many of the jobs were outsourced to firms which were new to the field and were based in remote villages. This resulted in lower out turn. With their experience, they struck to those job working firms who have shown improved results and hence the improvement in subsequent years. Their out-turn also depends on various factors like place of origin of the raw material, conditions in transit and storage, place where it is processed, the standing of the firm in business, skill sets of the work force, and condition of plant and machinery. The profit ratios also depend on the quality of output and demand in the market besides foreign exchange fluctuation. In light of these explanations, the assessee pleaded to ignore the small differences

found in the course of survey and volunteered to declare a sum of Rs. 1 crore as additional income for the A.Ys.2010- 11 to 2013-14.

7. However, the AO on the basis of some job work reports found at the time of survey which revealed that the yield derived is in the range of 22% and on the basis of excess cash and deficit cash found at the time of survey was of the view that production and sale outside the books cannot be ruled out. The AO confronted to the Assessee the above facts and directed the Assessee to enhance declaration of income to Rs.1,88,19,010/- for A.Y.2010-11 and file revised return declaring the additional income of Rs.1,10,33,440/- for A.Y.2010-11 by adopting yield @ 21%. The Assessee did accordingly and the same was accepted by the AO. In respect of the addition so made penalty proceedings u/s 271(1 )(c) were initiated.

8. The AO imposed penalty on the assessee holding that assessee concealed particulars of income and furnished inaccurate particulars of income.

9. On appeal, the CIT(Appeals) cancelled the order imposing penalty observing as under:-

“14 The addition made in this case is mainly on account of low gross profit and low yield declared in the books. Admittedly, in the assessment order the AO also mentioned that the appellant has maintained regular books of account with supporting documents. The only basis on which the additional income was offered was that the comparative cases are showing higher yields

and that for the A.Y.2013-14 the worksheets found at the time of survey were showing higher yield than that of the yield shown in the books for the A.Y.2010-11. The appellant's explanation that the yield and gross profit depends on various factors narrated elsewhere in the order was not accepted by the AO and finally, the assessment was concluded by adopting via media yield between 19.85% as per books and 22% as per the work sheets pertaining to A.Y.2013-14 and by adopting yield at 21% which was accepted by both the parties. From the assessment order and from the written submissions of the appellant it is clear that no supporting incriminating material or anything like that was found despite survey and finally the assessment was based on estimation only. It is settled legal position that levying of penalty depends on facts and circumstances of each case and is not automatic. Under the given facts and circumstances, in the absence of any concealment detected, the additions are based on comparison of yields with some other concerns and the yield of subsequent year which though was contested initially, was accepted at via media estimated percentage of 21%, I find strength in the argument of the appellant that the work sheets relied on pertain to A.Y. 2013-14 for which year the yield is claimed to be in line with these sheets, these documents cannot be termed as incriminating evidence. It is also pointed out that no separate additions were made with regard to excess cash found or deficit stock in the order since the addition is on agreed basis to cover up everything. From these set of facts, I am of the view that there cannot be scope for penalising the appellant since no concealment perse is detected and no inaccurate particulars are noticed. Hence the AO is directed to delete the penalty.”

10. Aggrieved by the order of CIT(Appeals), the Revenue has preferred the present appeal before the Tribunal.

11. We have heard the submissions of the Id. DR, who relied on the order of AO.

12. The Id. counsel for the assessee relied on the order of CIT(Appeals) and brought to our notice the show cause notice issued by the AO u/s. 274 of the Act before imposing penalty on the assessee, which does not spell out as to whether penalty was being levied for concealment of particulars of income or for furnishing inaccurate particulars of income. Our attention was drawn to the decision of the Hon'ble High Court of Karnataka in the case of *CIT & Anr. v. Manjunatha Cotton and Ginning Factory*, 359 ITR 565 (Karn) wherein the Hon'ble High Court held that notice u/s. 274 of the Act should specifically state as to whether penalty is being proposed to be imposed for concealment of particulars of income or for furnishing inaccurate particulars of income. In the absence of a specific mention as above, it was held that penalty imposed is liable to be cancelled.

13. We have considered the rival submissions. The Hon'ble Karnataka High Court in the case of *CIT & Anr. v. Manjunatha Cotton and Ginning Factory (supra)* has laid down the following principles to be followed in the matter of imposing penalty u/s.271(1)(c) of the Act.

“NOTICE UNDER SECTION 274

59. As the provision stands, the penalty proceedings can be initiated on various ground set out therein. If the order passed by the Authority categorically records a finding regarding the existence of any said grounds mentioned therein and then penalty proceedings is initiated, in the notice to be issued under Section 274, they could conveniently refer to the said order which contains the satisfaction of the authority which has passed the order. However, if the existence of the conditions could not be

discerned from the said order and if it is a case of relying on deeming provision contained in Explanation-1 or in Explanation-1(B), then though penalty proceedings are in the nature of civil liability, in fact, it is penal in nature. In either event, the person who is accused of the conditions mentioned in Section 271 should be made known about the grounds on which they intend imposing penalty on him as the Section 274 makes it clear that assessee has a right to contest such proceedings and should have full opportunity to meet the case of the Department and show that the conditions stipulated in Section 271(1)(c) do not exist as such he is not liable to pay penalty. The practice of the Department sending a printed form where all the ground mentioned in Section 271 are mentioned would not satisfy requirement of law when the consequences of the assessee not rebutting the initial presumption is serious in nature and he had to pay penalty from 100% to 300% of the tax liability. As the said provisions have to be held to be strictly construed, notice issued under Section 274 should satisfy the grounds which he has to meet specifically. Otherwise, principles of natural justice is offended if the show cause notice is vague. **On the basis of such proceedings, no penalty could be imposed on the assessee.**

60. Clause (c) deals with two specific offences, that is to say, concealing particulars of income or furnishing inaccurate particulars of income. No doubt, the facts of some cases may attract both the offences and in some cases there may be overlapping of the two offences but in such cases the initiation of the penalty proceedings also must be for both the offences. But drawing up penalty proceedings for one offence and finding the assessee guilty of another offence or finding him guilty for either the one or the other cannot be sustained in law. It is needless to point out satisfaction of the existence of the grounds mentioned in Section 271(1)(c) when it is a sine qua non for initiation or proceedings, the penalty proceedings should be confined only to those grounds and the said grounds have to be specifically stated so that the assessee would have the opportunity to meet those grounds. After, he places his version and tries to substantiate his claim, if at all, penalty is to be imposed, it should be imposed only on the grounds on which he is called upon to answer. It is not open to the authority, at the time of imposing penalty to impose penalty on the grounds other than what assessee was called upon to meet. Otherwise though the initiation of penalty proceedings may be valid and legal, the final order imposing

penalty would offend principles of natural justice and cannot be sustained. **Thus once the proceedings are initiated on one ground, the penalty should also be imposed on the same ground. Where the basis of the initiation of penalty proceedings is not identical with the ground on which the penalty was imposed, the imposition of penalty is not valid. The validity of the order of penalty must be determined with reference to the information, facts and materials in the hands of the authority imposing the penalty at the time the order was passed and further discovery of facts subsequent to the imposition of penalty cannot validate the order of penalty which, when passed, was not sustainable.**

61. The Assessing Officer is empowered under the Act to initiate penalty proceedings once he is satisfied in the course of any proceedings that there is concealment of income or furnishing of inaccurate particulars of total income under clause (c). Concealment, furnishing inaccurate particulars of income are different. Thus the Assessing Officer while issuing notice has to come to the conclusion that whether is it a case of concealment of income or is it a case of furnishing of inaccurate particulars. The Apex Court in the case of Ashok Pai reported in 292 ITR 11 at page 19 has held that concealment of income and furnishing inaccurate particulars of income carry different connotations. The Gujarat High Court in the case of MANU ENGINEERING reported in 122 ITR 306 and the Delhi High Court in the case of VIRGO MARKETING reported in 171 Taxman 156, has held that levy of penalty has to be clear as to the limb for which it is levied and the position being unclear penalty is not sustainable. Therefore, when the Assessing Officer proposes to invoke the first limb being concealment, then the notice has to be appropriately marked. Similar is the case for furnishing inaccurate particulars of income. The standard proforma without striking of the relevant clauses will lead to an inference as to non-application of mind.”

14. The final conclusion of the Hon'ble Court was as follows:-

“63. In the light of what is stated above, what emerges is as under:-

- a) Penalty under Section 271(1)(c) is a civil liability.
- b) Mens rea is not an essential element for imposing penalty for breach of civil obligations or liabilities.
- c) Willful concealment is not an essential ingredient for attracting civil liability.
- d) Existence of conditions stipulated in Section 271(1)(c) is a sine qua non for initiation of penalty proceedings under Section 271.
- e) The existence of such conditions should be discernible from the Assessment Order or order of the Appellate Authority or Revisional Authority.
- f) Even if there is no specific finding regarding the existence of the conditions mentioned in Section 271(1)(c), at least the facts set out in Explanation 1(A) & (B) it should be discernible from the said order which would by a legal fiction constitute concealment because of deeming provision.
- g) Even if these conditions do not exist in the assessment order passed, at least, a direction to initiate proceedings under Section 271(1)(c) is a sine qua non for the Assessment Officer to initiate the proceedings because of the deeming provision contained in Section 1(B).
- h) The said deeming provisions are not applicable to the orders passed by the Commissioner of Appeals and the Commissioner.
- i) The imposition of penalty is not automatic.
- j) Imposition of penalty even if the tax liability is admitted is not automatic.
- k) Even if the assessee has not challenged the order of assessment levying tax and interest and has paid tax and interest that by itself would not be sufficient for the authorities either to initiate penalty proceedings or impose penalty, unless it is discernible from the assessment order that, it is on account of such unearthing or enquiry concluded by authorities it has resulted in payment of such tax or such tax liability came to be

admitted and if not it would have escaped from tax net and as opined by the assessing officer in the assessment order.

l) Only when no explanation is offered or the explanation offered is found to be false or when the assessee fails to prove that the explanation offered is not bonafide, an order imposing penalty could be passed.

m) If the explanation offered, even though not substantiated by the assessee, but is found to be bonafide and all facts relating to the same and material to the computation of his total income have been disclosed by him, no penalty could be imposed.

n) The direction referred to in Explanation IB to Section 271 of the Act should be clear and without any ambiguity.

o) If the Assessing Officer has not recorded any satisfaction or has not issued any direction to initiate penalty proceedings, in appeal, if the appellate authority records satisfaction, then the penalty proceedings have to be initiated by the appellate authority and not the Assessing Authority.

p) Notice under Section 274 of the Act should specifically state the grounds mentioned in Section 271(1)(c), i.e., whether it is for concealment of income or for furnishing of incorrect particulars of income

q) Sending printed form where all the ground mentioned in Section 271 are mentioned would not satisfy requirement of law.

r) The assessee should know the grounds which he has to meet specifically. Otherwise, principles of natural justice is offended. On the basis of such proceedings, no penalty could be imposed to the assessee.

s) Taking up of penalty proceedings on one limb and finding the assessee guilty of another limb is bad in law.

t) The penalty proceedings are distinct from the assessment proceedings. The proceedings for imposition of penalty though emanate from proceedings of assessment, it is independent and separate aspect of the proceedings.

u) The findings recorded in the assessment proceedings in so far as "concealment of income" and "furnishing of incorrect particulars" would not operate as res judicata in the penalty proceedings. It is open to the assessee to contest the said proceedings on merits. However, the validity of the assessment or reassessment in pursuance of which penalty is levied, cannot be the subject matter of penalty proceedings.

The assessment or reassessment cannot be declared as invalid in the penalty proceedings.”

15. It is clear from the aforesaid decision that on the facts of the present case that the show cause notice u/s. 274 of the Act is defective as it does not spell out the grounds on which the penalty is sought to be imposed. Following the decision of the Hon'ble Karnataka High Court, we hold that the order imposing penalty has to be held as invalid.

16. Apart from the above, we are of the view that addition in respect of which penalty was imposed by the AO was only on low yield declared in the books of account. It is fundamental that before relying on the comparative results of other assessees in similar line of business, books of accounts of assessee should be found to be defective and there should be non-availability of yield percentage, accepted by the Revenue in assessee's own case in the past. In the case of assessee, it appears that reasons for adopting yield prevailing in the industry was due to discrepancy found in the form of excess cash admittedly at the time of survey and deficit stock of cashew kernels. It therefore appears to us that the very basis of estimation of income in the case of assessee is on a weak footing. It is a

different matter that assessee has accepted the order of AO without challenging the same. The fact remains that there was no detection of concealment either at the time of survey or thereafter. We are therefore of the view that the CIT(Appeals) was justified in cancelling the penalty imposed by the AO on the assessee. We do not find any grounds to interfere in the order of CIT(Appeals).

17. Consequently, appeal by the Revenue is dismissed.

Pronounced in the open court on this 14<sup>th</sup> day of August, 2015.

Sd/-

( ABRAHAM P. GEORGE )  
Accountant Member

Sd/-

( N.V. VASUDEVAN )  
Judicial Member

Bangalore,  
Dated, the 14<sup>th</sup> August, 2015.

/D S/

Copy to:

1. Appellant
2. Respondents
3. CIT
4. CIT(A)
5. DR, ITAT, Bangalore.
6. Guard file

By order

Assistant Registrar /  
Senior Private Secretary  
ITAT, Bangalore.