The State
v.
Dittu Ram

Bhandari, C. J.

the words "sufficient cause"' should receive a liberal construction so as to advance substantial justice when no negligence or inaction or want of *bona fides* is imputable to the appellant. It was held further that delay in the filing of an appeal ought not to be excused unless there are special circumstances, namely, a misleading by the other side or a mistake in the office itself or some sudden accident which could not be foreseen. Delay in the present case is sought to be condoned on the ground that the papers concerning this case were mislaid in the office. This case does not appear to me to fall within the ambit of the expression "sufficient cause" and the only order that can be passed in the circumstances is that the appeal must be dismissed. I would order accordingly.

Falshaw, J.

FALSHAW, J.—I agree.

INCOME-TAX REFERENCE.

Before Khosla and Kapur, JJ.

M/s. PANDIT BROS., Chandni Chowk, Delhi,—*Petitioner.*

versus

THE COMMISSIONER OF INCOME-TAX, DELHI,—*Respondent.*

Income-Tax Case (Civil Reference) No. 19 of 1953.

1954

March, 24th

Indian Income-tax Act, (XI of 1922)—Section 13 proviso—Conditions for its application—No stock account maintained—Whether entitles the Income-tax Officer to make additions to the book version of business profits on the sole ground that the net profits disclosed appear to be insufficient in relation to the total turn-over.

Held, that the wording of the proviso to section 13 makes it quite clear that before the Income-tax Officer can reject the final statement of profit and loss given by the assessee he must either hold that there is no method of accounting or that the method employed is such that it does not disclose the true profits and losses of the firm.

Held, that in all cases which fall under section 13 there must be material before the Income-tax Officer to lead him to the conclusion that the method employed is defective or that the case requires reconsideration and a new computation must be made. The fact that the profits appeared to him to be insufficient and the fact that there was no stock register maintained by the assessee are not such material upon which a finding can be given that the case falls within the proviso to section 13, but these are circumstances which may provoke an inquiry.

Held, that in order to make an increase in the profits the Income-tax Officer must adopt a basis. The statute gives the Income-tax Officer the power to determine his own basis, but there must be a basis.

Held, that the Income-tax Officer is not entitled to make an addition to the book version of business profits where no stock account is maintained, on the sole ground that the net profits disclosed appear to be insufficient in relation to the total turnover.

Civil Reference under Section 66(1) of the Indian Income-tax Act of 1922, has been referred to this Court by the Income-tax Appellate Tribunal (Delhi Bench), consisting of Shri K. N. Rajagopal Sastri, Judicial Member and Shri A. L. Sehgal, Accountant Member, dated the 8th June 1953, for decision of a question whether any addition may be made to the book version of business profits where no stock *account is maintained, on the sole ground that the net profits disclosed appear to be insufficient in relation to the total turn over.*

(R.A. No. 1260 of 1952-53).

(I.T.A. No. 5967 of 1951-52, Assessment year 1950-51)

D. K. KAPUR and R. K. GAUBA, for Petitioner.

A. N. KIRPAL and J. L. BHATIA, for Respondent.

JUDGMENT.

KHOSLA, J. (ORAL). This is a reference made to this Court by the Income-tax Appellate Tribunal, Delhi, under section 66(1) of the Income-tax Act. Khosla, J.

M/s. Pandit Bros., Chandni Chowk, Delhi

v.

The Commissioner of Income-tax, Delhi

Khosla, J.

The following question of law has been referred to this Court:—

> "Whether any addition may be made to the book version of business profits where no stock account is maintained, on the sole ground that the net profits disclosed appear to be insufficient in relation to the total turn over?"

The assessee in this case is Messrs. Pandit Bros., Delhi, and the year of assessment is 1950-51. In order to understand the exact import of the issue involved it is necessary to set out briefly the facts which have given rise to this reference.

Messrs. Pandit Bros. had, during the assessment year, four branches—

(a) Chandni Chowk, Delhi;

(b) Connaught Place, New Delhi;

(c) Handicrafts, New Delhi; and

(d) The Mall, Simla.

Accounts of these four branches were maintained separately but since they were all owned by the same firm a consolidated statement of total profit and loss was prepared for the information of the Income-tax Officer. The Income-tax Officer on going through the accounts found that taxable profits should have been declared at a higher figure. He examined the accounts of each separate branch and accepted the statements given by the firm in respect of the Old Delhi and the Simla branches. With regard to the branch known as Handicrafts, New Delhi, he was of the opinion that since no stock book had been maintained by the firm the

M/s. Pandit Bros., Chandni Chowk, Delhi
v.
The Commissioner of Income-tax, Delhi

Khosla, J.

gross profits were liable to be increased by a sum of Rs. 5,000. The exact words of his order are important and I quote them—

> "There is no stock book and it is not possible to verify that the whole of the stock was accounted for. I would increase the gross profit by Rs. 5,000 which would turn the gross loss of Rs. 1,872 into a net profit of Rs. 3,128."

A similar addition of Rs. 7,000 to the net profits was made in respect of the fourth branch Connaught Place, New Delhi, In respect of this branch the Income-tax Officer observed—

> "There is no stock book and it is not possible to verify that the whole of the stock is accounted for. I would increase the gross profit by Rs. 7,000. The net profit would thus work to Rs. 8,073."

In the course of his order the Income-tax Officer observed that the expense ratio for these two branches was unusually high as compared to the expense ratio obtaining at the Old Delhi branch. This was one of the reasons he gave for increasing the taxable figure of profits. An appeal was preferred to the Appellate Assistant Commissioner and by a brief order he dismissed the appeal. He observed—

> "And the profits disclosed keeping in view the quality of goods sold by the assessee and the inflatory tendencies in the market were insufficient.
>
> The expense ratio was very high. The employees appear to be paid not exactly on business-like principles—there appears to be a lot of philanthropic motives behind the very high payments

M/s. Pandit Bros., Chandni Chowk, Delhi
v.
The Commissioner of Income-tax, Delhi

Khosla, J.

made to them which are disproportionate to their qualifications and the nature of work done by them. They would not be able to get anywhere near the remunerations which the assessee is paying to them anywhere else in the open market. Only those expenses are allowable which can be brought down to strictly business principles. Philanthropy and business are strangers.

"The disallowance of Rs. 5,000 and Rs. 7,000 made by the Income-tax Officer to bring the results up to the normalities appear to be in order.

The matter was taken up again on appeal to the Income-tax Appellate Tribunal. The Tribunal also upheld the decision of the Income-tax Officer and seemed to take the view that the salaries, bonus and dearness allowance paid to the staff amounted to a large figure.

It is somewhat strange that the increase did not represent the figure which according to the Income-tax Officer, had been paid to the employees *mala-fide*. Indeed, there was no determination of such figures by him or by any of the appellate tribunals. The Income-tax Appellate Tribunal drew attention to this circumstance and observed—

"It may be that an assessee is not a good businessman and pays larger salary to his employees. What has to be found by the Income-tax authorities is whether the payment made is wholly and solely for the purposes of the assessee's business."

Therefore the Income-tax Appellate Tribunal did observe that the increase could not be made on this ground. The order of the Income-tax Officer was upheld for the following reasons given by the Tribunal:—

> "There is no proper records of the goods sold. As the profit disclosed by the assessee in the year under reference is extremely low, we think that the Income-tax authorities are right in making an estimate of the appellant's income under the proviso to section 13. Dealing with the estimate made as a whole, i.e., a net business income of Rs. 26,597 on a total turn over of about Rs. 9 lakhs, we think a very reasonable estimate has been made by the Income-tax authorities."

It is clear from these orders that two considerations were responsible for these decisions. In the first place, the Income-tax Officer, the Appellate Assistant Commissioner and the Income-tax Appellate Tribunal took the view that the profits disclosed by the firm were low. In the second place, they were influenced by the fact that no stock register had been maintained. It is clear that the account books maintained by the firm were accepted as correct, for the Income-tax Officer does not anywhere say that he rejected these account books. After the dismissal of his appeal by the Income-tax Appellate Tribunal the assessee moved the Tribunal for the statement of the case to this Court under section 66. The case was stated and the question which has been set out in the earlier part of my judgment was drawn up and sent to this Court for decision.

M/s. Pandit Bros., Chandni Chowk, Delhi
v.
The Commissioner of Income-tax, Delhi

Khosla, J.

It will be clear from what I have said that the increase was made under the proviso to section 13 of the Income-tax Act. This proviso is in the following terms:—

> "Provided that, if no method of accounting has been regularly employed, or if the method employed is such that, in the opinion of the Income-tax Officer, the income, profits and gains cannot properly be deduced therefrom, then the computation shall be made upon such basis and in such manner as the Income-tax Officer may determine."

The wording of this proviso makes it quite clear that before the Income-tax Officer can reject the final statement of profit and loss given by the assessee he must either hold that there is no method of accounting or that the method employed is such that it does not disclose the true profits and losses of the firm. In this case there was a method of accounting employed and therefore, the first part of the proviso does not apply. The question, therefore, arises whether the second part of the proviso is attracted. It is admitted that the assessee in this case has maintained regular accounts of his purchases and sales and these account books were accepted as correct. One thing was, however, missing namely a stock register. This in the opinion of the Income-tax Officer was an important document. The Income-tax Officer could have said that the absence of the stock register was such a serious defect in the method of accounting employed by the assessee that in his opinion he could not determine the correct statement of profits and losses. He could then have adopted some basis and computed the true

M/s. Pandit Bros., Chandni Chowk, Delhi
v.
The Commissioner of Income-tax, Delhi

Khosla, J.

profit taxable in a manner which he could determine under the proviso. In all cases which fall under section 13 there must be material before the Income-tax Officer to lead him to the conclusion that the method employed is defective or that the case requires reconsideration and a new computation must be made. As observed by their Lordships of the Privy Council in *The Commissioner of Income-tax, Bombay Presidency and Aden* v. *The Sarangpur Cotton Manufacturing Co., Ltd., of Ahmedabad*, (1).

> "It is the duty of the Income-tax Officer, where there is such a method of accounting, to consider whether the income, profits and gains can properly be deduced therefrom, and to proceed according to his judgment on this question."

The grievances of the assessee in this case are that (1) there was no finding by the Income-tax Officer that the method employed by him was improper or that the account books could not be relied upon as disclosing a true state of affairs, and (2) he did not compute the taxable profit on any basis as required by the proviso to section 13.

I have been at some pains to quote the exact words employed by the Income-tax Officer and the appellate tribunals who dealt with this case. There is no finding that there was material before the Income-tax Officer to lead him to the conclusion that a proper statement of income, profits and gains could not be deduced from the material placed before him. All he said was that the profits appeared to be somewhat low and there was

(1) I.L.R. 1938 Bom. 239

M/s. Pandit Bros., Chandni Chowk, Delhi
v.
The Commissioner of Income-tax, Delhi

Khosla, J.

no stock register. In my view the fact that the profits are low is merely a warning to him to look into the accounts more carefully and see whether there is material to lead him to the conclusion that there is some thing false in the account books. The mere fact that the profits are low is not material upon which a finding under section 13 can be based, because the assessee may be incompetent or his methods of business may be uneconomic. Again, the fact that there is no stock register only cautions him against the falsity of the returns made by the assessee. He cannot say that merely because there is no stock register the account books must be false. The account books in this case were accepted as correct and disclosing a true state of affairs. The absence of one register cannot amount to material and there must be material before the Income-tax Officer before he can apply the provisions of the proviso to section 13.

Again, we find that the Income-tax Officer did not adopt any basis for the increase made by him. He merely took what has been described by the Privy Council in *The Commissioner of Income-tax* v. *Kameshwar Singh*, (1) as a "leap in the dark" in adding the two items of Rs. 5,000 and Rs. 7,000 to the statement of profits as given by the assessee. The Income-tax Officer could have adopted one of many courses. He could have taken a test period from the assessee's own business and computed the true profits on that basis, or he could have considered the profits made by similar firms doing similar business, but it is not for this Court to indicate what method the Income-tax Officer should have adopted. The statute gives the Income-tax Officer the power to determine his own basis, but there must be a

(1) (1933) 1 I.T.R. 94

basis. He must not act in a wholly arbitrary manner. This has been pointed out in a number of cases and reference may be made to a recent decision of the Nagpur High Court in *Seth Nathuram Munnalal* v. *Commissioner of Income-tax* (2), where the following observations occur at Page 220:—

> "If after rejecting the method of accounting employed by the assessee, the Income-tax Officer were simply to add a particular amount to the income returned or to disallow a part of the business expenses properly incurred by the assessee and allowable under section 10 of the Act he would not be acting under the proviso to section 13. The Income-tax Officer would be acting contrary to law if he were to disallow such business expenses or make an addition of lump sum simply on the ground that the trading profits cannot be properly determined from the books of account. The Income-tax Officer is not entitled to discard the evidence of the books of account altogether merely because the proviso to section 13 is attracted."

In this case it was conceded that the account books did not disclose the true state of affairs and that case therefore was much weaker from the assessee's point of view than the case before us.

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(1) (1953) 25 I.T.R. 216

M/s. Pandit Bros., Chandni Chowk, Delhi
v.
The Commissioner of Income-tax, Delhi

Khosla, J.

In another case *A. Moosa and Sons, Bombay* v. *Commissioner of Income-tax, Bombay City*, (1), Chagla, C.J., observed—

> "The proviso to section 13 leaves it to the Income-tax Officer to compute the profits upon such basis and in such manner as he may determine. Although the discretion is vested in the Income-tax Officer, the discretion cannot be exercised arbitrarily or capriciously or dishonestly. He must exercise his judgment in such a manner as would make it possible for him to ascertain the profits and gains of the assessee most approximating to the truth."

His Lordship observed later—

> "Therefore it is always open to the Court on a reference to consider whether the method adopted by the Income-tax Officer is a wrong method, wrong in the sense that the method is not one which is likely to result in the true profits and gain being ascertained."

A reference is made to an observation of Earl Loreburn L.C., which I have already quoted above. In that case the assessee had maintained no stock account and in the statement of the case made by the Income-tax Appellate Tribunal the following significant observation appears:—

> "The Tribunal necessarily does not reject the accounts in the absence of a stock account in all cases. It takes into account various other factors and the history of the assessee's past assessments. It is only after a careful consideration of all the facts that a finding is given that

(1) (1953) 23 I.T.R. 73

> the assessee's books do not disclose his true profits, or that proviso to section 13 applies."

This observation made by the Income-tax Appellate Tribunal is all the more significant as pointing out the duties laid upon the Income-tax Officer in applying the provisions of section 13. In that case the question referred to the High Court was—

> "Whether there was material before the Tribunal to come to a finding that the assessee's books do not disclose his true profits?"

In dealing with this question Chagla, C.J., made an inquiry into whether the method adopted by the Income-tax Officer was a just and proper method. The case before us is of a similar nature and here, too, we must inquire whether the addition of the two items of Rs. 5,000 and Rs. 7,000 was made according to some just and definite basis. We find that no basis is mentioned and no method was adopted by the Income-tax Officer. All he did was to express an opinion that the profits were unduly low and therefore needed to be increased, and on this he proceeded to increase them by a sum of Rs. 12,000. This is scarcely acting according to the provisions of the statute.

I, therefore, find that in this case there is no definite finding by the Income-tax Officer that the case falls within the proviso to section 13, for he does not say that the method of accounting employed by the assessee was such that in his opinion "the income, profits and gains could not properly be deduced therefrom." In the second place, even if such a finding were to be implied from his order it cannot be said that there was material before him which would enable him to come to this finding. The fact that the profits appeared to him to be insufficient and the fact that there was

M/s Pandit Bros., Chandni Chowk, Delhi
v.
The Commissioner of Income-tax, Delhi

Khosla, J.

no stock register maintained by the assessee are not in my view materials upon which such a finding can be given, but these are circumstances which may provoke an inquiry. The Income-tax Officer must discover evidence or material *aliunde* before he can give such a finding. In the third place, I find that in increasing the taxable income he did not adopt any method or basis.

For these reasons I would answer the question referred to us in the negative. The assessee will recover costs. I assess counsel fee at Rs. 100.

Kapur, J.

KAPUR, J. I agree.

APPELLATE CIVIL.

Before Khosla and Kapur, JJ.

THE CENTRAL BANK OF INDIA, LTD.,—*Appellant.*

versus

RAM SARUP KHANNA AND ANOTHER,—*Respondents.*

Regular Second Appeal No. 64-D of 1953

1954

March, 25th

Contract—Triparty—Whether could be revoked by one of the parties to it—Estoppel—When operates—Rule stated.

G. P. note held by R. S. endorsed by him to the Bank. On 9th September, 1946, R. S. wrote to the Bank that its amount be handed over to S. P. with interest and that he had no right, title and interest in the note. S.P. took this letter to the Bank. On 19th September, 1946, S.P. asked the Bank to pay him the amount due under the note or an advance against it. Bank advanced Rs. 2,000 to S.P. against the note. On 27th September, 1946, R.S. wrote to the Bank cancelling previous instructions, dated 9th September 1946. Thereafter, the Bank realized the amount of the note and