

IN THE HIGH COURT OF DELHI

Date of decision : April 28, 1998

CWP NO. 1913 OF 1998

M/S. SUPER CASSETTES INDUSTRIES LTD.....
through: Mr G.C. Sharma, Sr Adv.
with Mr Anoop Sharma, and
Mr T.R.Talwar
Advocates

Versus

ASSISTANT COMMISSIONER OF INCOME TAX.....
through: Mr R.D.Jolly Sr Standing Counsel
with Ms Premlata Bansal
Advocate

CORAM :-

THE HON'BLE MR JUSTICE R.C. LAHOTI
THE HON'BLE MR JUSTICE MUKUL MUDGAL

1. Whether reporters of Local papers may be allowed to see the judgment ? —
2. To be referred to the reporter or not ? YES

R.C. Lahoti, J.

The Assistant Commissioner of Income-tax Act has by his order dated 31.3.1998, subject to previous approval by the CIT, directed special audit under Section 142(2A) of the Income-tax Act, 1961 to be conducted on his forming an opinion that having regard to the nature and complexity of the accounts and interest of revenue, it was a fit case for such audit. The aggrieved petitioner has filed this petition under Articles 226/227 of the Constitution of India seeking the quashing of the abovesaid order.

2. The principal submission of Shri G.C. Sharma, the learned Senior Advocate for the petitioner, has been that in view of the total sales in business of the petitioner having exceeded Rs. 40



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lakhs, the accounts of the petitioner have already been audited as ordained by Section 44AB of the Act and hence there was no occasion for directing the special audit. It was further submitted that sub-section (2A) in Section 142 was introduced by the Taxation Laws (Amendment) Act, 1975 with effect from 1.4.1976. However, Section 44AB has been introduced by the Finance Act, 1984 w.e.f. 1.4.1985 which provides for compulsory audit of accounts in certain cases wherein the petitioner would be included on account of its total sales exceeding Rs. 40 lakhs. Introduction of Section 44AB does away with the need of special audit under sub-section (2A) of Section 142 and renders the provision redundant to the extent of the cases covered by Section 44AB. The proforma prescribed for audit report under Section 142(2A) and one under Section 44AB are similar, submitted the learned counsel, which fact lends strength to the argument of redundancy. Strong reliance was placed on a Division Bench decision of A.P. High Court in A.S. Sarma & ors v. UOI (1989) 175 ITR 254 and the single Bench decision of Rajasthan High Court in Abhey Kumar & Co vs. UOI (1987) 164 ITR 148.

3. The senior standing counsel for the respondent who has entered appearance on advance notice offering to oppose the admission itself of the petition, has submitted that Section 44 AB does neither overrule nor render redundant, wholly or



partially, the Section 142 (2A) of the Act. The two provisions operate independent of each other and hence can co-exist. The petition is, therefore, devoid of any merit and is liable to be dismissed, submitted the learned counsel for respondent.

4. The order dated 31.3.1998, Annexure-I, is accompanied by a copy of "brief notes" placed on the record by the assessing officer. We may draw the relevant facts therefrom.

4.1 The assessee is a limited company deriving income from manufacturing and sale of audio cassettes, video cassettes, TV, compact discs and related components. Return declaring Nil income was filed on 30th November, 1995. On total sales of Rs.97.08 crores, profit of Rs.7.18 crores has been disclosed, but after claiming deductions u/s 80 HH, 80 HHC, 80I and 80IA, net income has been shown at Nil.

4.2 Assessee has claimed royalty expenses of Rs. 49.03 lakhs. These expenses are lump-sum payment for acquisition of rights of songs of various films purchased from various producers during the year. After purchase of rights, a catalogue number is given to a particular song and its production is made and sales are disclosed.



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4.3 The assessing officer has formed an opinion which in his own words is as under :-

"I have come to the conclusion that having regard to the nature and complexity of the accounts of the assessee and the interest of the revenue, it is a fit case to be referred to special audit u/s 142 (2A) of the I.T. Act.

The special auditor is required to verify with the records maintained by the assessee quantitative details with mention of catalogue number and sales with mention of each catalogue number. The special auditor is required to file break-up of sales relating to audio and video cassettes manufactured in earlier years with mention of catalogue number. The special auditor is required to file its report in respects of quantitative details regarding purchases, sales production with reference to cost of raw material, consumption of electricity expenses, generator, labour employed etc.

Special auditor is required to verify the claim of the assessee that each unit is independent with other units and expenses claimed in units and head office are relevant to the particular unit only. It should also be certified that the profits declared in units are correct or not or inter-dependent with other units, especially with reference to various inter-unit transfer of stock components."

4.4 During the course of his notes, the assessing officer has observed that in spite of several opportunities having been allowed for the purpose, the assessee was not in a position to file quantitative analysis/details of very many relevant things including the following :-

- i) of audio cassettes with mention of production, sales, closing stock, sales realisation;
- ii) of closing stock and production in respect of audio cassettes manufactured



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in earlier years;

- iii) of cassettes manufactured in earlier years but sold in current year;
- iv) of closing stock of product in respect of video cassettes manufactured in earlier years;
- v) of machines with details as to make and capacity and maximum production which could be made from these machines;

and so on.

4.5 At one place the assessing officer records in his brief notes :-

"Assessee has disclosed profit of Rs. 6.44 crores on total sales of Rs. 16.66 crores in Namoli unit whereas in other units losses has been shown. There is no manufacturing activity at Namoli. Only manual assembly of parts is being claimed here just to claim deductions u/s 80HH and 80I. It is found that all the parts of audio cassettes are transferred from other units of the company and some parts are taken from sister concern and huge profits are shown from this unit. All the expenses are booked in other unit and only nominal expenses are booked in this unit. From the expenses claimed in this unit it gives the impression that assessee is earning more than 6 crores without any expenses in this unit. There is no business on earth except gambling and speculation which can generate such profit with a nominal expenses as claimed in this unit. It is found that this is nothing but only by inter unit transfer and book adjustment assessee is showing abnormal profit from this unit.

From the accounts it is found that there are entry transfer of goods from one unit to other just to increase profits of some units to increase profits abnormally.

In head office a loss of Rs. 1.36 crores has been claimed. There is no purchase or sale in head office. Head office is not a unit but most of the expenses are claimed in head office whereas these expenses related to various units.

Assessee is claiming that each unit is



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independent and actual profits are shown on the basis of audit report. But it is found that stock of components is transferred and adjusted in such a manner that abnormal profits are shown in some units to claim deductions. Namoli unit is about 25 Km from Noida. Assessee has admitted only assembly of blank audio cassettes manually there and all the components are transferred from other units. Only nominal expenses are claimed in Namoli unit but profits of Rs. 6.44 crores on manual assembly of blank audio cassettes are shown, just to claim deductions u/s 80HH and 80I. Intention of the legislature is to encourage manufacturing activity in particular areas. Intention of the legislature is not to encourage diversification of assembly work from existing units to other units just to claim deductions u/s 80HH and 80I. Similar is the case in the case of Unit at C.25 and unit at C26 also. It is found that sales are adjusted according to the deductions/exemptions available to the assessee without any corresponding manufacturing activity. Inter unit transfers of components are shown to increase or decrease profits.

Thus in this case sales are not verifiable. Production is also not verifiable with reference to capacity of machines and consumption of electricity expenses, generator expenses, labour employed and consumption of raw material."

5. In our opinion on the facts found prima facie, no fault can be found with the assessing officer having taken a decision to initiate special audit under Section 142(2A).

6. We may now proceed to test the validity of the submission that Section 44AB has replaced and rendered redundant Section 142(2A) to the extent of the cases covered by the former provision. The submission of the learned senior counsel is based on



hereinabove.

7. In A.S. Sarma's case (supra) vires of explanation-I to Section 44AB were under challenge. In that context, the learned judges have made various observations. At the end of page 262 the Division Bench has observed:-

It is further contended that section 44AB is superfluous as recourse to Section 142(2A) of the Act serves the purpose. Section 142(2A) enables the assessing authority to direct the accounts to be audited in the event of complexity of accounts. ~~(This power can be exercised in respect of all complexity of accounts.)~~ This power can be exercised in respect of all assessees. The stipulation of compulsory audit is evidently conceived with the twin purposes of having vigilance of the accounts of the assessees in higher income brackets to detect evasion if any and lubricating expeditious assessment. The power under Section 142(2A) can be invoked when the assessing authority finds that the accounts are complicated and it must be stated that in view of section 44AB, the recourse to section 142(2A) is confined to assessees having turnover or transactions below Rs. 40 lakhs or gross professional receipts below Rs. 10 lakhs. The overlapping in certain situations does not render the provision invalid or superfluous and the contention is untenable."

7.1 We have two observations of our own to make. Firstly, the para begins with noting the contention advanced and ends with the observations of the court. We are not sure if any other sentence excepting the last one is the observation of the court. Secondly, the holding of the court is that overlapping in certain situation does not render the provisions invalid or superfluous. We fail to



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appreciate how does it strengthen the plea of the petitioner.

8 . In Abhay Kumar & Co's case (supra) validity of Section 44 AB and Section 271 B of the Income-tax Act were under challenge. The learned Judge also interpreted Section 44AB. The emphasis was on the question whether this Section was applicable to commission agents or not. The petitioner therein were commission agents. During the course of his judgment, the learned Judge has observed:-

"The assessee is not put to double jeopardy in having to get his accounts audited once under section 142(2A) and again under Section 44AB. In fact, Section 142(2A) was a dormant provision which was to be invoked in a given situation that has been made explicit by incorporating the same in section 44AB. The two provisions are consistent."

8.1 In our opinion, even this observation does not advance the petitioner's case before us. The learned Judge has held the two provisions to be consistent and not hit by the rule of double jeopardy. The specific object behind enacting sub-section (2A) into Sec.142 is to assist the assessing officer in framing an assessment when he finds the accounts of the assessee to be complex, by having the services of a special auditor at hand. Special audit can also be ordered so as to protect the interest of the revenue. Such objects may or may not be achieved by the audit contemplated by Section



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44AB.

9. In the case at hand the detailed note put up by the assessing officer though styled as brief note provides a forceful illustration of a case where in spite of an audit under section 44AB resort to special audit under Section 142(2A) becomes a must. We have also perused form No. 3CD and form 6B referable to Ss.44AB and 142(2A). In our opinion the latter form contemplates more intensive information being made available to the assessing officer than what is done by the former. Moreover, it is fallacious to assume that the report of special auditor appointed u/s 142 (2A) shall remain necessarily confined to the prescribed proforma. The Assessing Officer may instruct the special auditor to provide information on specific points over and above the statutory report. This is what has been done in the case at hand. The 'Brief Note' put up by the assessing officer shows what are the aspects or points on which special auditor has to report additionally.

10. In M/S Ramesh Chand Industries Ltd v. UOI, (CWP 1580/98 decided on 2.4.1998) turning down a challenge to special audit under section 142(2A) we have held:

"A bare reading of the provision shows that all that is required for initiation



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of special audit is formation of the opinion that it is necessary so to do dependent on the availability of the abovesaid two facts. The provision does not use the words "reason to believe". Recording of reasons is not an essential requirement of the provision. The assessing officer must obtain previous approval of the Chief Commissioner or the Commissioner. The intervention of such a high ranking authority is an inbuilt protection to the assessee against any arbitrary or unjust exercise of the power by the assessing officer. It is not the case of the petitioner that such previous approval of the Chief Commissioner or the Commissioner has not been obtained. There is no allegation of malafides. This court would not in exercise of its writ jurisdiction sit in appeal over the formation of the opinion by the assessing officer."

11. We are, therefore of the opinion that no case is made out for interfering with the impugned order referring the petitioner to special audit.

The petition is dismissed.


R.C.LAHOTI, J.

APRIL 28, 1998


MUKUL MUDGAL, J.

VSP