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* **HIGH COURT OF DELHI AT NEW DELHI**

% **Date of Decision: 16th August, 2010**

\+ **ITA NO.1132/2010**

COMMISSIONER OF INCOME TAX ..... Appellant

Through: Mrs. Prem Lata Bansal, Adv.

versus

RAM LAL GUPTA ..... Respondent

Through: None.

AND

\+ **ITA NO.1134/2010**

COMMISSIONER OF INCOME TAX ..... Appellant

Through: Mrs. Prem Lata Bansal, Adv.

versus

RAM LAL GUPTA ..... Respondent

Through: None.

AND

\+ **ITA NO.1136/2010**

COMMISSIONER OF INCOME TAX ..... Appellant

Through: Mrs. Prem Lata Bansal, Adv.

versus

RAM LAL GUPTA ..... Respondent

Through: None.

AND

\+ **ITA NO.1139/2010**

COMMISSIONER OF INCOME TAX ..... Appellant

Through: Mrs. Prem Lata Bansal, Adv.

versus

RAM LAL GUPTA ..... Respondent

Through: None.

+ **ITA NO.1141/2010**

COMMISSIONER OF INCOME TAX ..... Appellant

Through: Mrs. Prem Lata Bansal, Adv.

versus

RAM LAL GUPTA ..... Respondent

Through: None.

AND

+ **ITA NO.1138/2010**

COMMISSIONER OF INCOME TAX ..... Appellant

Through: Mrs. Prem Lata Bansal, Adv.

versus

RAJ KUMAR GUPTA ..... Respondent

Through: None.

AND

+ **ITA NO.1144/2010**

COMMISSIONER OF INCOME TAX ..... Appellant

Through: Mrs. Prem Lata Bansal, Adv.

versus

RAJ KUMAR GUPTA ..... Respondent

Through: None.

CORAM:
HON'BLE THE CHIEF JUSTICE
HON'BLE MR. JUSTICE MANMOHAN

1. Whether reporters of the local papers be allowed to see the judgment? Yes
2. To be referred to the Reporter or not? Yes
3. Whether the judgment should be reported in the Digest? Yes

DIPAK MISRA, CJ

This batch of appeals preferred under Section 260A of the Income Tax Act, 1961 (for brevity 'the Act') by the revenue is directed against the order dated 19th June, 2009 passed by the Income Tax Appellate Tribunal, New Delhi Bench 'E' (for short 'the tribunal') in ITA Nos. 1306 and 1307/Del/2009 pertaining to the

assessment years 2005-06 and 2006-07 and ITA Nos. 1308, 1309, 1310, 131 1312/Del/2009 relating to the assessment years 2002-03, 2003-04, 2004-05, 2005-06 and 2006-2007 respectively.

2. The revenue in the memorandum of appeal has raised the following substantial questions of law:-

a) Whether ITAT was correct in law in deleting the addition made by AO invoking provisions of Section 40A(3) of the Act on account of cash purchases?

b) Whether ITAT was correct in law in holding that where the AO had made addition applying gross profit rate then no separate addition u/s 40A(3) could be made?

c) Whether order passed by ITAT is perverse in law whether it deleted the addition ignoring that the scope of Section 145 and Section 40A(3) are distinct and they are not overlapping?

3. We have heard Mrs. Prem Lata Bansal, learned counsel for the appellant-revenue on the question of admission.

4. To appreciate whether the questions raised by the learned counsel for the revenue really involve substantial questions of law, it is apposite to refer to certain essential facts. Be it noted that in all the appeals similar questions have been framed and the factual matrix is the same and that is why the tribunal has disposed of all the appeals by a composite order. For the sake of clarity and convenience we thought it apt to adumbrate the facts from ITA No.1132/2010.

5. The assessee is the proprietor of M/s Mangal & Co. It earns commission as arhatiyas by procuring agriculture commodities for mill owners. The return of

Rs.1,08,87,617/-. He had shown Rs.48,000/- as income from salary 1,08,73,280/- as income from business and Rs.311/- as income from other sources. A notice under Section 143(2) of the Act was issued on 14th June, 2006 and a set of questionnaires was issued along with the notices under Sections 142(1) and 143(2) on 8th October, 2007 and 16th October, 2007. The assessee replied to the questionnaires. It was contended by the assessee that it was the Kachha Arhatiyas acting on commission basis through his proprietary firm and payment was made in cash as per the practice prevalent in market. It was put forth that the turnover was only the commission and does not include the sales on behalf of the others/principals and for that purpose reliance was placed on auditors report and tax audited accounts. It was the stand of the assessee that it was engaged in procurement of agriculture commodities mainly wheat and channa as arhatia from agriculturists or cultivators of the produce from the States of U.P. and Rajasthan for commission and they do not have any kind of domain over the goods. It was set forth that the major procurement of agriculture commodities was used by M/s Shree Bankey Behari Exports Limited and M/s Deluxe Cold Storage & Food Processors Limited. The goods procured from the cultivators were supplied at a price at which they were procured i.e. without making any value addition or provision of profit to the cost of such goods procured during arhatiyas business activities and purchase was not assessee's expenditure and hence not subjected to tax under provisions of Section 40A(3).

6. The assessing officer posed certain issues, namely whether the activity of the assessee is to act as Kachha Arhatiyas or is involved in trading activities; whether all the purchase made from farmers are genuine or not and whether cash payments

provisions contained in Section 40(A)(3) of the Act. After posing the ques the assessing officer adverted to the stand put forth by the assessee and rejected the books of accounts and computed the income of the assessee at Rs.4,94,992/- after applying of net profit rate of 0.05% and further initiated a proceeding under Section 271(1)(c) of the Act on the ground that the assessee had furnished inaccurate particulars. The assessing officer also came to hold that the purchases are not reflected in the books of accounts and, hence, the results shown in the said books could not be accepted and under these circumstances, the assessee was not covered by exemptions stated under Rule 6DD of the Rules and disallowance under Section 40A(3) to the extent of 20% of the purchases deserve to be computed. It is worth noting that the assessing officer held that the assessee had failed to produce the farmers and, hence, genuineness of purchase from the farmers was in doubt and, therefore, it could be safely concluded that he was not a Kaccha Arhita but engaged in trading activity. Because of this, the assessing officer also initiated a penalty proceeding and imposed a demand and charged interest under Sections 234A, 234B, 234C and 234D of the Act.

7. Being dissatisfied with the aforesaid order, the assessee preferred an appeal before the CIT(A). The CIT(A) took note of the fact that a search and seizure operation under Section 132 was conducted on 20th December, 2005; that the procurement of agriculture produce was made from two sources; that the assessing officer was fully satisfied that the cost paid thereof by the sister concerns is fair market price; that the quantity stated as procured through the appellant is duly reflected as purchase in the books of the above referred assessee; that the rejection of books of accounts by the assessing officer was absolutely justified; that adding

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reasonable; and that determination of net income of Rs.4,94,392 did not w interference. Thereafter, the CIT(A) came to hold as follows:-

> "If the appellant's case is examined in the light of the above circular, it is noticed that the appellant's nature of business falls under the ambit of kachha arhatiya. The appellant has not purchased the agriculture produce for earning profit by making sale of goods. The appellant has earned only commission on the transaction of procurement. The appellant's responsibility was only to represent for the mill owners before the agriculturists at the time of procurement of goods for the third party. The appellant does not have any dominion over the goods and was entitled solely for commission and not interested in the profits/loss in the transactions. Thus it can be said that the appellant was engaged in the business as kachhha arhatiya."

8. Thereafter, the CIT(A) adverted to other aspects and other facts to substantiate the conclusion that the assessee was engaged in the business of kachha arhatiya and he was a commission agent and, therefore, provisions of Section 40(A)(3) is not applicable on payments made for procurement of food grains and, therefore, no disallowance under Section 40(A)(3) be made.

9. After adverting to the said aspects the first appellate authority undertook an exercise that even if the appellant is the pacca arhatiya engaged in the business of purchase and sale of agriculture produce for earning profits and not as a purely commission agent, he had made the procurement of agriculture produce from the farmers / cultivators by making payment in cash. He had produced books of accounts before the assessing officer in that regard and filed an affidavit before the assessing officer clearly stating that he had procured the agriculture produce such as channa and wheat from the agriculturists or cultivators from the States of U.P., Haryana and Rajasthan. There is no material on record to suggest that agriculture produce was not procured from the farmers. The assessee had produced material on record in that regard and the material included the names of the persons and the

Roller Flour Mills for the said agriculture produce after charging a commissi 0.50 paise per bag. This would go a long way to show that he had procured the food grains, namely, wheat, channa, etc. from the farmers / cultivators. After referring to the said aspect, the CIT(A) referred to Rule 6DD which stipulates that the cases and circumstances in which payment in a sum exceeding Rs.20,000/- may be made otherwise than by an account payee cheque drawn on a bank or account payee bank draft. On the aforesaid basis, the CIT(A) also came to the conclusion that in the case of the assessee the agriculture produce was procured by him on making payment to cultivators / growers of the agriculture produce and he falls within the exception of Rule 6DD and, hence, excluded from the purview of Section 40A(3) of the Act.

10. On a perusal of the order passed by the tribunal it is noticeable that the tribunal has held as follows:

> "A perusal of the assessment order also clearly shows that the Assessing Authority has rejected the books of accounts of the assessee in page 5 Para 7 of the assessment order and also estimated the business income of the assessee. Since the books of accounts are rejected, the books of accounts no more retain evidentiary value. The books of accounts also remain outside the scope for verification since the same are rejected. Since the books of accounts are rejected and the same are not available for scrutiny, obviously the addition by invoking the provisions of Section 40A(3) of the Act cannot be made as the entries in the books of accounts are also not available for verification. In these circumstances, respectfully following the decision of the Third Member of this Tribunal in the case of India Seed House referred to supra, the findings of Ld. CIT(A) on this issue stand confirmed. In these circumstances, all these appeals of the revenue stand dismissed."

11. In this context, we may refer with profit to the decision in ***Shanti Lal v. Madan Lal and others*** AIR 1954 Allahabad 789 wherein the distinction between

the kachha arhatia and pakka arhatia has been succinctly drawn, which rea under:

> "19. There was controversy between the parties regarding the question as to whether the plaintiff was a 'pakka arhatia' or was only a commission agent or 'kachha arhatia'. The plaintiff contended that he was a 'pakka arhatia'. The answering defendants, on the other hand, contended that they were only commission agents and were liable to render accounts. The basis of the distinction between a 'kachha' and a 'pakka arhatia' is that a 'kachha arhatia' acts as an agent on behalf of his constituent and never acts as a principal to him. The person with whom he enters into a transaction on behalf of his constituent is either brought into contact with the constituent or at least the constituent is informed of the fact that the transaction has been entered into on his behalf with such and such other person. Although the 'kachha arhatia' may not communicate the name of his constituent to the third party, he informs the constituent of the name of the party. In the case of a 'pakka arhatia', the agent makes himself liable on the contract not only to the third party, but also to the constituent and he does not inform his constituent as to the person with whom he has entered into the contract on his behalf. In the present case the contract shows that the position of the plaintiff was that of a 'pakka arhatia'.
>
> In the case of a 'pakka arhat' transaction the real question is to ascertain what as between the parties was the real intention when they entered into the contract in question: Whether it was ever within their contemplation that goods should be delivered, or whether their real intention was only to pay a difference on or after the due date. The mere circumstance that in the printed contract form an opportunity is left open to the parties to complete their contract by actual delivery will not be allowed to deprive the Court of the power to consider whether that was their real intention. A contract may none the less be a contract by way of gaming or wagering because it purports to give the buyer or seller an option of demanding delivery or acceptance, as the case may be, of the subject matter of the contract. In short, the parties will not be allowed to "camouflage" their transaction by getting it up as a "delivery" transaction when, in fact, it was never their intention that it should be.
>
> We may in this connection refer to a decision of a Bench of this Court in – 'Firm Ram Krishna Das Jawahar Lal v. Firm Mutsaddi Lal Murli Dhar', AIR 1942 All 170 (T)."

12. It will not be out of place to refer to the CBDT Circular: No.452 [F. No.201/3/85-IT(A-II)], dated 17-3-1986. The same reads as follows:

"…. The Board have received representations from various persons, trade associations, etc., to clarify whether in cases where an agent effects sales/turnover on behalf of his principal, such sales/turnover have to be treated as the sales/turnover of the agent for the purpose of section 44AB.

3. The matter was examined in consultation with the Ministry of Law. There are various trade practices prevalent in the country in regard to agency business and no uniform pattern is followed by the commission agents, consignment agents, brokers, kachha arahtias and pacca arahtias dealing in different commodities in different parts of the country. *The primary necessity in each instance is to ascertain with precision what are the express terms of the particular contracts under consideration.* Each transaction, therefore, requires to be examined with reference to its terms and conditions and no hard and fast rule can be laid down as to whether the agent is acting only as an agent or also as a principal.

4. The Board are advised that *so far as kachha arahtias are concerned, the turnover does not include the sales effected on behalf of the principals and only the gross commission has to be considered for the purpose of section 44AB. But the position is different with regard to pacca arahtias*. A pacca arahtia is not, in the proper sense of the word, an agent or even *del credere* agent. The relation between him and his constituent is substantially that between the two principals. On the basis of various Court pronouncements, following principals of distinction can be laid down between a kachha arahtia and a pacca arahtia:

(1) A kachha arahtia acts only as an agent of his constituent and never acts as a principal. A pacca arahtia, on the other hand, is entitled to substitute his own goods towards the contract made for the constituent and buy the constituent's goods on his personal account and thus he acts as regards his constituent.

(2) A kachha arahtia brings a privity contract between his constituent and the third party so that each becomes liable to the other. The pacca arahtia, on the other hand, makes himself liable upon the contract not only to the third party but also to his constituent.

(3) Though the kachha arahtia does not communicate the name of his constituent to the third party, he does communicate the name of the third party to the constituent. In other words, he is an agent for an unnamed principal. The pacca arahtia, on the other hand, does not inform his constituent as to the third party with whom he has entered into a contract on his behalf.

(4) The remuneration of a kachha arahtia consists solely of commission and he is not interested in the profits and losses made by his constituent as is not the case with the pacca arahtia.

(5) The kachha arahtia, unlike the pacca arahtia, does not have any dominion over the goods.

(6) The kachha arahtia has no personal interest of his own when he enters into transaction and his interest is limited to the commission agent's charges and certain out of pocket expenses whereas a pacca arahtia has a personal interest of his own when he enters into a transaction.

(7) In the event of any loss, the kachha arahtia is entitled to be indemnified by his principal as is not the case with pacca arahtia.

5. The above distinction between a kachha arahtia and pacca arahtia may also be relevant for determining the applicability of section 44AB in cases of other types of agents. *In the case of agents whose position is similar to that of kachha arahtia, the turnover is only the commission and does not include the sales on behalf of the principals. In the case of agents of the type of pacca arahtia, on the other hand, the total sales/turnover of the business should be taken into consideration for determining the applicability of the provisions of section 44AB."*

13. In the case at hand the CIT(A) has analysed the facts and came to hold that the respondent – assessee had not purchased the agriculture produce for earning profit by making sale of goods but had only earned commission on the transaction of procurement. The assessee's responsibility was only to represent for the mill owners before the agriculturists at the time of procurement of goods for the third party. He had no dominion over the goods and was only entitled for commission. He was not concerned with the profits/loss in the transactions. That apart, the first appellate authority has also referred to the survey under Section 133A of the Act which was conducted by the investigation wing. The investigation report showed that the agriculturists had stated that they got all the sale payment in cash and clarified that they make sale of their agriculture produce through 'dalals' in the

assessee was engaged in the business of kachha arhatiya. The Tax Audit R under Section 44AB furnished with the original return under Section 139 also mentions that he was a commission agent. The assessee has not made any claim of expenses for the procurement of agriculture produce. In this background he has been treated as a commission agent and, therefore, Section 40A(3) is not applicable to him.

14. Be it noted, the CIT(A) as also the tribunal have also come to hold that payment made to cultivators or growers of the agriculture produce otherwise than by an account payee cheque or account payee bank draft is excluded from the purview of Section 40A(3) of the Act. Reference has been made to the decisions in ***Indwell Constructions v. CIT*** (1998) 232 ITR 776 (AP), ***CIT v. Purshottamlal Tamrakar*** (2004) 270 ITR 314 (MP), ***CIT v. Banwari Lal Banshidhar*** (1998) 229 ITR 229 (All.).

15. Judged from both the angles, we find that the orders passed by the CIT(A) and the tribunal are invulnerable and deserve the stamp of approval of this Court.

16. Consequently, we do not perceive any merit in this batch of appeals and they are dismissed in limine.

CHIEF JUSTICE

MANMOHAN, J

AUGUST 16, 2010
VK/nm