* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

\+ **ITA No.995/2009**

% **Date of Decision: 24.05.2011**

COMMISSIONER OF INCOME TAX .... **APPELLANT**

Through: Ms.Prem Lata Bansal, Sr. Advocate with Mr,Deepak Anand, Advocate

Versus

BETTERWAYS FINANCE & LEASING PVT. LTD. .... **RESPONDENT**

Through: Mr.M.S. Syali, Sr. Advocate with Mr.V.P. Gupta and Mr.Basant Kumar and Ms.Husnali Syali, Advocates for the respondent

CORAM:
HON'BLE MR. JUSTICE A.K. SIKRI
HON'BLE MR. JUSTICE M.L. MEHTA

1. Whether reporters of 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

A.K. SIKRI, J. (Oral)

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1. For the assessment year 2001-2002, the respondent/assessee filed its return declaring income of ₹3,67,26,812/-. While making the assessment, the Assessing Officer noticed that the assessee had taken a loan of ₹4.00 crores from M/s.Enam Securities Pvt.

Ltd and loan of ₹1.00 crore from M/s.Stratcap Investments Pvt. Ltd. vide agreements dated 14.04.2000 and 25.04.2000 respectively. As per these agreements, the assessee had also pledged 1,00,000 shares of M/s.DCM Asic Technology Limited with M/s.Enam Securities Pvt. Ltd. and 25,000 shares with M/s.Stratcap Investments Pvt. Ltd. Both the agreements, which were on identical terms, provided that in case of failure on part of the assessee to repay the loan along with 13.5% interest, the lenders were entitled to forfeit the shares pledged with them and on such forfeiture the entire loan amount along with interest was to be treated as repaid. The Assessing Officer found that in addition to the aforesaid one lakh and 25,000 shares pledged with the aforesaid two lenders respectively, additional shares to the tune of 50,000 and 12,500 shares of M/s.DCM Asic Technology Limited were also pledged with M/s.Enam Securities Pvt. Ltd. and M/s.Stratcap Investments Pvt. Ltd. on 01.10.2000. The explanation of the assessee was that as the value of the shares pledged with these lenders had fallen, the lenders had asked for further securities, which were accordingly given. The Assessing Officer, however, did not accept the aforesaid explanation of the assessee. He was of the view that when the original agreement clearly stipulated the pledge of one lakh and 25,000 shares, which meant that shares were valued at ₹400/-

per share, and the clauses in the agreements also stipulated forfeiture of these shares in the event assessee had failed to discharge the liability by repaying the loan, there was no occasion to given any pledge in further shares with the lenders. After rejecting the explanation, the Assessing officer formed the opinion that the assessee company had given 50,000 and 12,500 shares to the said two lenders in excess of its liability. On this premise and taking the value of each share at ₹400/-, he treated sum of ₹2.5 crores (62,500 x 400) as the income on account of long-term capital gain and added the same and made an addition of ₹2,50,01,273/- as long-term capital gain not offered for taxation. Against the order of the Assessing Officer, the assessee preferred appeal before the CIT(A). Along with the appeal, the assessee also filed application under Section 46(A) of the Income Tax Rules for admission of certain additional documents. The explanation given in this application was that these documents could not be submitted before the Assessing Officer as proper opportunities had not been given. To put it precisely, the case of the assessee was that when the justification for giving additional security was asked for by the Assessing Officer, the assessee had explained the same vide letters dated 10th December, 2003 and 19th February, 2004, but the Assessing Officer, thereafter, did not raise any further

queries. On this premise, plea was taken by the assessee that the assessee could not furnish the said correspondence which was exchanged between the assessee and the two lender companies as per which further security was agreed to be given. The CIT(A) called for the remand report. The remand report dated 08.09.2004 was furnished by the AO to the CIT(A). In this report, the AO stated that he had gone through the additional documents, however, the admissibility thereof was questioned by the Assessing officer on the ground that the original agreements dated 14.04.2000 and 25.04.2000 entered into between the assessee and two lenders respectively did not provide for giving additional security at subsequent dates and, therefore, reliance on the subsequent correspondence between the lender and the borrower could not be placed by the assessee. Significantly, the Assessing Officer did not challenge the veracity of these documents but questioned the admissibility thereof on the aforesaid terms. The CIT(A) after hearing the parties admitted the additional documents inter alia observing as under:

> "7. ... The appellant company vide application filed under Rule 46A had submitted that in response to query of the A.O. it had filed letter dated 10.12.2003 and 19.02.2004. The AO had required no further explanation/documents in regard to the transaction. Therefore, the

> appellant company could not submit full correspondence to him. The AO in his report has made no comments regarding the above claim of the appellant company. Since the AO was making substantial addition, he ought to have raised specific queries to the appellant company. In my opinion, therefore, the appellant company is entitled to submit additional documents as evidence. Accordingly, additional evidence is hereby admitted in the interest of justice."

2. Thereafter the CIT(A) discussed these documents. It observed that the Assessing Officer had not made any comments on merits in his remand report. Thus proceeding on this basis that the authenticity of these documents were not challenged, on the basis of these documents, he came to conclusion that the original documents entered into between the parties had been modified by these documents, whereby the assessee had agreed to pledge further shares by way of security. We may point out in this connection that within three days of the agreement entered into between the parties, the lender had written letter dated 17th April, 2000 mentioning therein that the security of one lakh shares was accepted by the lenders keeping in view the future growth plans of M/s.DCM Asic Technology Limited (the company of which shares were pledged) and it was clarified in this letter that if there is no fall in the performance of the said company vis-à-vis the business plan growth opportunities as

shown to the lenders, then the lenders would be free to ask for additional shares as additional security as per the said arrangement. The assessee had replied the same vide letter dated 19th April, 2000 confirming and undertaking that in case additional security is required in the circumstances narrated by the lenders, the assessee shall provide the same. Thereafter vide letter dated 1st October, 2000, the lenders had written to the assessee that the performance of the M/s.DCM Asic Technology Limited was not improving and in fact there were wide gap between provisional six monthly figures and projected estimates, because of this reason the lenders asked for additional security of 50,000 and 12,500 equity shares respectively of M/s.DCM Asic Technology Limited. It was on the basis of this correspondence exchanged between the parties whereby the assessee had agreed to provide additional security that ultimately the assessee pledged further shares with the two lender companies. Based on this correspondence exchanged between the parties, the CIT(A) came to the conclusion that the original agreement was mutually novated/modified by the lenders and the assessee and there was sufficient reason to believe the contentions of the assessee in this behalf. On this basis, the CIT(A) accepted the justification given by the assessee in giving the additional security. It is a matter of record that the assessee had pledged

to pay the loan amount along with interest, in liquidation of which both the lenders had forfeited the security which was now to the tune of 1,50,000 and 37,500 shares respectively and appropriated those shares by transferring the same in their respective names. In the process, CIT(A) relied upon the judgment of the Supreme Court in ***K.P. Varghese*** *v.* ***Income Tax Officer, Ernakulam and Anr.,*** 131 ITR 597. This led to the deletion of the addition made by the Assessing Officer.

3. The Revenue challenged this decision of the CIT(Appeal) before the Income Tax Appellate Tribunal. The said appeal has been dismissed by the ITAT holding that the CIT(Appeal) was justified in admitting the additional evidence and was also right in deleting the addition in view of the fact that the original agreement had been modified by the parties.

4. It is this order of the ITAT which is challenged by the Revenue in the instant appeal filed under Section 260A of the Income Tax Act. The Revenue has challenged the admission of additional documents produced by the assessee under Rule 46A of the Income Tax Rules before the CIT(A) as well as decision of the authorities below on merits deleting the additions made by the Assessing officer on account of long-term capital gain.

5. Coming to the issue of admitting the additional documents from the narration of events disclosed above, we are of the view that no fault can be found in the approach of the CIT(A) or the ITAT in this behalf. No doubt, the Assessing Officer had asked the assessee to justify the pledge of additional 50,000 and 12,500 shares with the two lenders respectively. The assessee had stated in detail in its statement as to in what circumstances on 1st October, 2000, the assessee was made to give the additional security. Thereafter, no further queries were raised by the Assessing officer. No doubt, while giving its explanation vide letter dated 10th December, 2003 and 19th February, 2004, the assessee could have taken care to annex these documents as well. However, when specific averments were made in the aforesaid explanation, at that time even the Assessing Officer should have enquired the matter further. However, the mistake which was committed by the Assessing Officer was that in view of the clauses contained in the original agreements, there was no scope and/or reason to provide additional security. Probably because of this reason, he did not enquire into the matter further and concluded that there was no room for providing additional security. It is trite law that the terms of contract entered into between the parties can be changed, altered, modified and even rescinded by further mutual agreements. Such a novation is

permissible as per Section 62 of the Contract Act. The CIT(Appeal) has also found justification in such a step taken by the parties. It is inter alia observed that during that period the value of shares of IT companies had suffered substantially and data of CNX IT index showed that fall in the value of IT companies was almost 50%. Even if we take the value of the share pledged at ₹400 at the time of entering into the original agreements, if it was fallen by 50%, in October 2000, the value would be ₹200/-. In these circumstances, even by giving additional security of 50000/12500 additional shares, it was a prudent act on the part of the assessee to ensure liquidation of the entire liability of ₹4.00 crores/₹1.00 crore along with interest which had accrued thereupon.

6. This Court in ***CIT*** v. ***Hewlett Packard India (P) Ltd.***, 314 ITR 55 (Del.) has held that admissibility of additional evidence by CIT(A) would not give rise to any substantial question of law, provided the CIT(A) or the Tribunal had not acted on any wrong principle.

7. Thus, insofar as admission of additional evidence is concerned, it was within the discretion of the CIT(A) to admit the said evidence and we find that in the instant case, the said discretion has not been exercised improperly or against the provisions of law.

8. Once we hold that the additional evidence given in the form of correspondence provided by the assessee was duly and properly admitted by the CIT(A), the question on merits as decided by the two authorities below does not pose any problem. It is stated at the cost of repetition that in the remand report, the Assessing Officer had not questioned the genuineness and veracity of the documents. Though he had specifically mentioned that the additional documents had been gone through and perused by him, he had only questioned the admission of these documents in view of Rule 46A of the Income Tax Act that too on the ground that the original agreements entered into between the assessee and the lenders did not provide for giving additional security on subsequent dates and for this reason alone, he contended that the assessee could not place reliance on subsequent correspondence. Therefore, CIT(Appeal) was right in proceeding on the premise that such a correspondence was in fact genuine and exchanged between the parties. Once this position is accepted coupled with the fact that the parties to the contract have agreed to change the terms thereof and it was actually done in the instant case, the furnishing of additional security became justified and there was no reason to treat the same as long-term capital gain, authorities below in this behalf have

rightly referred to the judgment of ***K.P. Verghese*** (supra) in arriving at this decision.

9. We are of the opinion that no question of law arises and the appeal is dismissed accordingly.

A.K. SIKRI, J.

MAY 24, 2011 **M.L. MEHTA, J.**
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