With Blessings of Devi Saraswati

"Impact of judgement of SC in the case of NRA Iron and Steel Pvt Ltd on Assessment/Appeal of Share Capital/Premium"

Presented by

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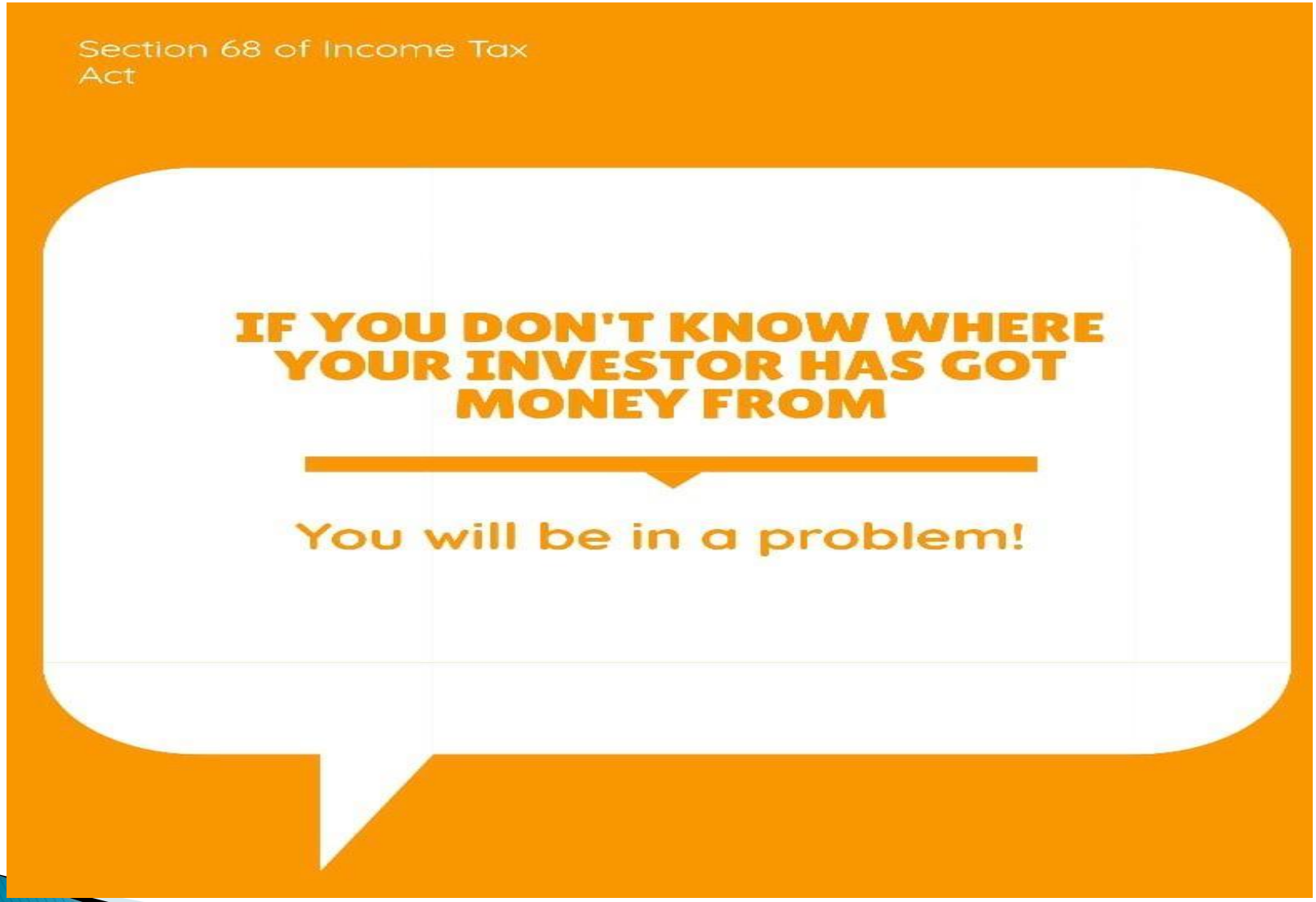
At Baroda Branch of ICAI

Welcome to all Members

Section 68 of Income Tax Act



CASE STUDY

Sherlock Holmes was sitting in a pensive mood, smoking his pipe. A puzzled Watson asked: "What is the matter ?"Holmes said: "My dear Watson, there is one case, which I also cannot solve."Watson was really curious: "Which one?" Sherlock Holmes replied: "I have been asked by a company In India to gather details about how much money each of it's investors has in bank. Even I cannot, gather such details about investors, using my detective skills !

Cash credits.

68. Where any sum is found credited in the books of an assessee maintained for any previous year, and the assessee offers no explanation about the nature and source thereof or the explanation offered by him is not, in the opinion of the [Assessing] Officer, satisfactory, the sum so credited may be charged to income-tax as the income of the assessee of that previous year :

[**Provided** that where the assessee is a company (not being a company in which the public are substantially interested), and the sum so credited consists of share application money, share capital, share premium or any such amount by whatever name called, any explanation offered by such assessee-company shall be deemed to be not satisfactory, unless—

(*a*) the person, being a resident in whose name such credit is recorded in the books of such company also offers an explanation about the nature and source of such sum so credited; and(*b*) such explanation in the opinion of the Assessing Officer aforesaid has been found to be satisfactory: **Provided further** that nothing contained in the first proviso shall apply if the person, in whose name the sum referred to therein is recorded, is a venture capital fund or a venture capital company as referred to in clause (*23FB*) of section 10.]

INTRODUCTION- SECTION 68

- Lethal weapon used by the Department against evasive tactics used by the assessees, to convert their unaccounted money in accounted one.
- Total Income under Chapter IV. (Sec. 14 to Sec. 59.) Five heads u/s 14.
- Sec. 14 starts with "save as otherwise provided by this Act".
- There are some other incomes which may not fall under these five heads, but aggregated while computing total income.
- Aggregation of income is in Chapter – VI (Sec. 66 to Sec. 69C.)
- Primarily such credit is not income and it may be any kind of transaction which is not income per se, but it is charged to income-tax as income of the assessee if assessee fails to offer an explanation or explanation offered by him is not in the opinion of the Assessing Officer satisfactory.

INTRODUCTION- CONT…

- Even prior to introduction of section 68, one may refer to the judgment of the Apex Court in case of Kale Khan Mohammad Hanif vs. CIT -[1963] 50 ITR 1 (SC), wherein the Court has held as under:

  > "It is well established that the onus of proving the source of a sum of money found to have been received by the assessee is on him. If he disputes liability for tax, it is for him to show either that the receipt was not income or that if it was, it was exempt from taxation under the provisions of the Act. In the absence of such proof, the Income-tax Officer is entitled to treat it as taxable income".

- Similar finding was given by the Apex Court in case of A. Govindarajulu Mudaliar vs. CIT – [1958] 34 ITR 807 (SC).
- It was only later that the above dictum of the Apex Court found embodiment in section 68 of the Act.
- Any credit appearing in the books of an assessee,
- Where the assessee is not able to or not satisfactorily able to explain the nature and source of such credit.

INTRODUCTION- CONT…

- It is a deeming fiction, whether or not the credit is otherwise income chargeable to tax.
- Initial onus is on the assessee to demonstrate the "nature and source" of the credit and after that, the burden shifts onto the Department to prove that the credit is income chargeable to tax.

  a. Identity of the creditor

  b. capacity of the creditor to advance money and

  c. genuineness of the transaction.

- The term 'any sum found credited' also takes under its sweep any sum credited as share capital, share premium or share application money or any such amount by whatever name called [Refer Sophia Finance Ltd – 205 ITR 98 (Del); CIT vs. Ruby Traders and Exporters Ltd. -263 ITR 300 (Cal); – CIT vs. Divine Leasing and Finance Pvt. Ltd. – 299 ITR 268 (Del)]
- Burden u/s. 68 has been, considerably modified after certain Court decisions in favour of Revenue [refer- Pr. CIT v. NRA Iron & Steel (P.) Ltd. [2019] 103 taxmann.com 48 (SC) and Pr. CIT v. NDR Promoters (P.) Ltd. [2019] 102 taxmann.com 182/410 ITR 379 (Delhi)].

INTRODUCTION- CONT…

- Emphasis on human probabilities.
- Why someone would invest in an unknown company to acquire shares at very high premium, or would give loan without security, as it is contrary to human behaviour, the addition u/s. 68 has been confirmed.
- Subjective decision of the AO, about the explanation submitted by the assessee along with documentary evidence in respect of his loan transaction or receipt of share capital with premium, leaving very little scope for an objective consideration.
- Decision about explanation furnished by the assessee, whether it is satisfactory or not, is primarily a question of discharge of onus lying on the assessee.
- Contrary to the law relating to discharge of burden settled u/s. 68, r.w.s. 106 of the Evidence Act.

Requisites of section 68 of the Income Tax Act

- Generally, the assessee submits various documents in support of his explanation,
  - PAN, bank statements of the investor, bank statement of the assessee, MOA and AOA of the investor companies, documents submitted with ROC for raising capital, financial statements of the investor companies for the relevant year and subsequent years, confirmation from the investor companies/lender, details of the present directors and their addresses of lender/investor companies, share applications, etc.
- Once, these documents are submitted, it has been held that assessee has discharged the primary onus lying on him. In the case of CIT v. Mohanakala [2007] 161 Taxman 169/291 ITR 278 (SC), "the assessee offers no explanation" appearing in Section 68 of the I.T. Act held that the expression means "where the assessee offers no proper, reasonable and acceptable explanation as regards the sum found credited in the books maintained by the assessee." [refer- CIT v. Smt. Arati Jana [2013] 35 taxmann.com 2/216 Taxman 109 (Cal.)]

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- **BURDEN OF PROOF:**
  - Section 101 of the Indian Evidence Act.
  - Whoever desires any Court to give judgment as to any legal right or liability dependent on the existence of facts which he asserts, must prove that those facts exist.
  - When a person is bound to prove the existence of any fact, it is said that the burden of proof lies on that person.
  - The general rule is that 'burden of proof is always on the party, who asserts a proposition or fact which is not self-evident.
  - The burden of proof has two shades of meaning. In the primary sense, it means the burden of establishing the case.
  - The second meaning of 'burden of proof is on the principle of evidence. In the second sense, the burden would be shifted from one party to the other, as and when adequate evidence to discharge the burden that lay on a party is being produced by that party. [refer- Dy. CIT v. Singla Enclave Developers (P.) Ltd. [2013] 40 taxmann.com 127/[2014] 149 ITD 177 (Chandigarh - Trib.)] Once burden is shifted to other party to the dispute, onus lies on that party to discharge the burden so shifted on him.

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- Under Cash credit, the burden of proof is not a static.
- The initial burden of proof lies on the assessee. Amount appearing in the books of account of the assessee is considered a proof against him. He can discharge this burden by submitting evidence as listed above. Once the assessee produces evidences about identity and creditworthiness of the lender and genuineness of transaction, the burden of proof shifts to the revenue. [refer- ITO v. Anant Shelters (P.) Ltd. [2012] 20 taxmann.com 153/51 SOT 234 (Mum.)].
- The Revenue can examine all the evidences, carry out inquiry and investigation to infer that identity and creditworthiness of the creditor are doubtful and, therefore, genuineness of transaction cannot be believed.
- On the basis of evidence collected by the AO, the burden is shifted back on the assessee who is required to rebut doubt, like furnishing correct and new address of the creditor, data from ROC/MCA portal about existence of the investor company, assessment orders of the investor companies, any other document where existence of the investor company is proved by action taken by other Government Department.
- Where creditworthiness is doubted by the AO on account of low income of the investor company, the burden is discharged by the assessee by producing balance sheets and showing heavy assets and liabilities of the investor companies.

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- **CASE LAWS ON BURDEN OF PROOF:**
  - The term explanation to the nature and source leads to the burden of proof. The law is well-settled that the onus of proving the source of a sum of money found to have been received by an assessee is on him. Where the nature and source of a receipt, whether it be of money or other property, can not be satisfactorily explained by the assessee, it is open to the revenue to hold that it is the income of the assessee and no further burden lies on the revenue to show that the income is from any particular source. Roshan Di Hatti v. CIT [1977] 107 ITR 938 (SC).

  - Where the assessee has failed to prove satisfactorily the source and nature of the credit entry in his books and it is held that the relevant amount is the income of the assessee, it is not necessary for the department to locate the exact source. The same was also held in the case of CIT v. M. Ganapathi Mudaliar [1964] 53 ITR 623 (SC).

Contrary evidence by the Assessing Officer

- If the explanation offered by the assessee about the nature and source thereof, in the opinion of the Assessing Officer is not satisfactory or the Assessing Officer is not satisfied with such explanation and produces some prima facie evidence against the explanation of the assessee. Like, there is receipt of money in the books of assessee and assessee gives an explanation and the Assessing Officer presents some other evidence which is not matching with the explanation given by the assessee, the assessee has to rebut the same. If assessee fails to do so, the said evidence being unrebutted can be used against him by holding that it is a receipt of income in nature. Sumati Dayal v. CIT [1995] 80 Taxman 89/214 ITR 801 (SC).

Prerequisites to satisfy the Assessing Officer

- The decision of the Delhi High Court in CIT v. Lovely Exports Pvt. Ltd. [2008] 299 ITR 268 (Delhi) has explained the prerequisites to satisfy the Assessing Officer wherein it was held that:
  - "In the case of a company the following are the propositions of law under section 68. The assessee has to prima facie prove:
- (1) the identity of the creditor/subscriber;
- (2) the genuineness of the transaction, namely, whether it has been transmitted through banking channel or other indisputable cannels;
- (3) the creditworthiness or financial strength of the creditor/subscriber;
- (4) if relevant details of the address of PAN identity the creditor/subscriber along with copies of the shareholders register, share application forms, share transfer register, etc, it would constitute acceptable proof or acceptable explanation by the assessee;
- (5) the Department would not be justified in drawing an adverse inference only because the creditor/subscriber fails or neglect to respond to its notice;
- (6) The Assessing Officer is duty bound to investigate into the creditworthiness of the creditor/subscriber, the genuineness of the transaction and the veracity of the repudiation."
- These six points have been highlighted by the Hon'ble Delhi High Court based on the facts of the case but point nos. (1), (2), (3) and (6) are applicable invariably in all cases.

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- The Hon'ble Delhi High Court in CIT v. Oasis Hospitalities Pvt. Ltd. [2011] 9 taxmann.com 179/198 Taxman 247/333 ITR 119 (Delhi), held that :
  - "The initial onus is upon the assessee to establish three things necessary to obviate the mischief of Section 68. Those are:
    - (i) identity of the investors;
    - (ii) their creditworthiness/investments; and
    - (iii) genuineness of the transaction.

The departments exercise starts only when these three ingredients are established prima facie, by the assessee and the department is required to investigate into the facts presented by the assessee.

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- In CIT v. P. Mohankala [2007] 161 Taxman 169 (SC)/[2007] 291 ITR 278 (SC), Court held that:
  - A bare reading of section 68 of the Income-tax Act, 1961, suggests that

(i) There has to be credit of amounts in the books maintained by the assessee;

(ii) Such credit has to be a sum of money during the previous year; and

(iii) Either (a) the assessee offers no explanation about the nature and source of such credits found in the books, or (b) the explanation offered by the assessee, in the opinion of the Assessing Officer, is not satisfactory. It is only then that the sum so credited may be charged to Income-tax as the income of the assessee of that previous year. The expression "the assessee offers no explanation" means the assessee offers no proper, reasonable and acceptable explanation as regards the sums found credited in the books maintained by the assessee

Simply disowning the explanation of the assessee without producing any contrary evidence, it cannot be said that the AO is not satisfied. In the case of Lovely Exports, it was categorically said by the Hon'ble Delhi High Court that "The Assessing Officer is duty bound to investigate into the creditworthiness of the creditor/subscriber the genuineness of the transaction and the veracity of the repudiation".

What if the transaction is routed through bank account

- The question that often arises is that whether it necessary to prove the creditworthiness, genuineness and identity of the creditor, if such transaction is routed through the proper banking channel? The Allahabad High Court in the case of CIT v. Smt. Prem Lata Sethi [2014] 220 Taxman 333/[2013] 40 taxmann.com 492 (All) held that transaction through bank account is not enough to explain creditworthiness of creditor and genuineness of transaction. This should be separately investigated into by the AO.

- The Hon'ble Patna High Court in the case of Addl. CIT v. Bahri Bros [1985] 154 ITR 244/22 Taxman 3 said that the question of identity of the creditor is irrelevant if it is routed through the proper banking channel.

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Assessee furnishes the PAN of the creditor

- The question also arises whether it is sufficient if the assessee furnishes the name, address and PAN of the creditor? The Hon'ble Calcutta High Court in the case of CIT v. Korley Trading Co. Ltd. [1998] 232 ITR 820, held that where without filing confirmation letter from the creditor, the assessee merely mentioned the PAN No of the creditor, the genuineness of such transaction can not be said to have been proved by the assessee.

Assessee furnishes the confirmation letter

- If the assessee produces confirmation letter from the creditors, can it be said that assessee has discharged its onus to prove the identity, creditworthiness and geniuses of the transaction? The confirmation letter can be said to be a good evidence only when the creditors had also declared the amounts in their income-tax return which were accepted by the AO. Jalan Timbers v. CIT [1997] 223 ITR 11/90 Taxman 298 (Gau)
- In the recent judgment of Pr. CIT v. NRA Iron & Steel (P.) Ltd. [2019] 103 taxmann.com 48 (SC), it was held that the initial onus is upon the assessee to establish three things necessary to obviate the mischief of Section 68. Those are:

  (i) identity of the investors;

  (ii) their creditworthiness/investments; and

  (iii) genuineness of the transaction.

  and the assessee-Company failed to discharge the onus required under Section 68 of the Act, the Assessing Officer was justified in adding back the amounts to the Assessee's income.

Requisites of section 106 of Evidence Act

- Section 106 is designed to meet certain exceptional cases in which it would be impossible, or at any rate disproportionately difficult for the prosecution to establish facts which are "especially" within the knowledge of the accused and which he could prove without difficulty or inconvenience. The word "especially" means facts that are pre-eminently or exceptionally within his knowledge. The burden of proving the facts which are especially in the knowledge of a party is on that party. The burden to establish those facts, which are especially in his knowledge is cast on the person concerned and if he fails to establish or explain those facts, an adverse inference of facts may arise against him. [refer- Collector of Customs v. D. Bhoormal [1974] 2 SCC 544].
- Applies to Assessee and Revenue both.
- If the Revenue wants to rely on certain facts which are especially and only in the knowledge of the Revenue, then the burden is on the Revenue to prove the existence of such facts.

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- In a case where a Private Limited company or an individual takes credit from certain private parties (either as loan or share capital) then the knowledge about the party (lender/investor) will be especially in the knowledge of the assessee.
- The burden is on the assessee to identify such party with adequate evidence.
- The burden is limited to proving identity and existence of that party. A direction by the AO to the assessee to produce the lender/investor, as the lender/investor is personally known to the assessee does not fall in the category of a fact and, therefore, section 106 cannot be invoked to take adverse view against the assessee in case he is unable to produce the lender/investor. No power is given by law to the assessee to enforce the attendance of lender/investor.
- It is the identity and address of the lender/investor which is a fact which can be said to be especially known to the assessee. Once identity and existence of the lender/investor is proved beyond doubt, the burden would shift on the Revenue to prove otherwise by enforcing attendance/survey/commission/search as they are vested by the law with enormous powers.
- The burden u/s. 106 of the Indian Evidence Act is confined to fact and not to procedure. in Nemi Chand Kothari v. CIT [2004] 136 Taxman 213[2003] 264 ITR 254 (Gau.) held that "section 68 of Income-tax Act, should be read along with section 106 of Evidence Act." Therefore, onus on the assessee "should be decided by taking into consideration the provision of section 106 of the Evidence Act which says that a person can be required to prove only such facts which are in his knowledge."

Reliance on section 106 of the IE Act by the Tribunal/Court

- In several cases, as below the Courts/Tribunals have relied upon section 106 of the IE Act for restricting the scope of burden lying on the assessee and enlarging the burden of the Revenue. These cases are-
  - (i) CIT v. Shiv Dhooti Pearls & Investment Ltd. [2015] 64 taxmann.com 329/[2016] 237 Taxman 104 (Delhi) - assessee is liable to disclose only source(s) from where he has himself received credit and it is not burden of assessee to show source(s) of his creditor nor is it burden of assessee to prove creditworthiness of source(s) of sub-creditors. The Proviso to section 68 inserted by the Finance Act, 2012 w.e.f. 1-4-2013 has modified this proposition under which investor-company/individual is required to explain the nature and source of its investment made in the assessee-company (closely held company) as share application money, share capital, share premium or such similar amount.
  - (ii) CIT v. Sanjay Jain [2015] 55 taxmann.com 512/230 Taxman 550 (Cal.) - In a case where sale proceeds in cash from sale of shares was credited in the books then the burden to disclose the name of the person to whom the shares were sold, sale note issued by a broker are in the special knowledge of the assessee and the alleged buyer and the alleged debtor. Assessee could have adduced evidence which was in his special knowledge which is also the requirement of law in Section 106 of the Evidence Act.

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- (iii) Dhanraj Mills (P.) Ltd. v. Asstt. CIT [2014] 52 taxmann.com 464/[2015] 152 ITD 253 (Mum. - Trib.) - Where the books of account of the assessee show the transaction as purchase and sale of securities, this fact is within the special knowledge of the assessee itself, therefore, the burden of proving this fact squarely lies upon the assessee.

Difference between section 68 of the IT Act and section 106 of the IE Act

- In this regard the observations of the Tribunal in ITO v. Wiz-Tech Solutions (P.) Ltd. [IT Appeal No. 1162/Kol/2015 (C Bench)] are relevant. "…… section 106 of the Evidence Act limits the onus of the assessee to the extent of his proving the source from which he has received the cash credit, section 68 gives ample freedom to the Assessing Officer to make inquiry not only into the source(s)of the creditor but also of his (creditor's) sub-creditors and prove, as a result, of such inquiry, that the money received by the assessee, in the form of loan from the creditor, though routed through the sub-creditors, actually belongs to, or was of, the assessee himself. In other words, while section 68 gives the liberty to the Assessing Officer to enquire into the source/source from where the creditor has received the money, section 106 makes the assessee liable to disclose only the source(s) from where he has himself received the credit and it is not the burden of the assessee to prove the creditworthiness of the source(s) of the sub-creditors. If section 106 and section 68 are to stand together, which they must, then the interpretation of section 68 has to be in such a way that it does not make section 106 redundant.“
- "The burden of the assessee to prove the genuineness of the transactions as well as the creditworthiness of the creditor must remain confined to the transactions, which have taken place between the assessee and the creditor. What follows, as a corollary, is that it is not the burden of the assessee to prove the genuineness of the transactions between his creditor and sub-creditors nor is it the burden of the assessee to prove that the sub- creditor had the creditworthiness to advance the cash credit to the creditor from whom the cash credit has been eventually received by the assessee. It, therefore, further logically follows that the creditor's creditworthiness has to be Judged vis-a-vis the transactions, which have taken place between the assessee and the creditor, and it is not the business of the assessee to find out the source of money of his creditor or of the genuineness of the transactions, which took between the creditor and sub-creditor and/or creditworthiness of the sub-creditors, for these aspects may not be within the special knowledge of the assessee."

Effect of combined reading of section 68 of the IT Act and section 106 of the IE Act

- (i) Where certain facts are in the special knowledge of the Department such as search at the premises of entry operators, statement of entry operators, documents indicating involvement of the assessee in obtaining accommodation entry, then burden is on the Department to bring those evidences on record and confront to the assessee. The assessee cannot be asked to disprove a fact which is not proved by the Department.
- (ii) The burden of the Department under Section 106 is to prove that the sum so credited is only an entry as this fact is especially within its knowledge.
- (iii) Where certain fact is as much available to the prosecution, the facts cannot be said to be "especially" within the knowledge of the accused.
- (iv) Section 106 cannot come into play where the facts concerned are such as are capable of being known by other also.
- (v) Discharge of the onus on the assessee "should be decided by taking into consideration the provision of section 106 of the Evidence Act which says that a person can be required to prove only such facts which are in his knowledge."
- (vi) "The assessee/borrower cannot be called upon to explain, much less prove the affairs of the creditor, which he is not even supposed to know or about which he cannot be held to be accredited with any knowledge."

(CONT..)

- (vii) The burden u/s. 68 lying on the assessee shall remain confined to the transactions, which have taken place between the assessee and the creditor. It is not the burden of the assessee to prove the genuineness of the transactions between his creditor and sub-creditors nor is it the burden of the assessee to prove that the sub- creditor had the creditworthiness to advance the cash credit to the creditor from whom the cash credit has been eventually received by the assessee.
- (viii) While the Assessing Officer under section 68, is free to look into the source(s) of the creditor and/or of the sub-creditor, the burden on the assessee under section 68 is definitely limited.
- (ix) Section 106 makes the assessee liable to disclose only the source(s) from where he has himself received the credit. It is not the burden of the assessee to prove the creditworthiness of the source(s) of the sub-creditors.
- (x) In a case where AO finds that the transaction between creditor and sub-creditor is not genuine and sub-creditor had no creditworthiness, it will not necessarily mean that the loan advanced by the sub-creditor to the creditor was income of the assessee from undisclosed source unless there is evidence, direct or circumstantial, to show that the amount which has been advanced by the sub-creditor to the creditor, had actually been received by the sub-creditor from the assessee

Effect of human probabilities

- Even in a case where assessee is able to place all the documents on record on identity of the creditor and its creditworthiness, still there are certain factors which would create doubt over genuineness of the transaction. For example, (i) where investor receives money in its bank account but is not able to prove the source of it (covered by Proviso to Section 68), (ii) though the investor/lender was existing at the time of transaction but thereafter it is lost in oblivion, no trace is found on any Government portal, why would somebody lose forever his precious money in favour of the assessee, (iii) charging of high premium on share application when group to which assessee belongs, has no goodwill, it is not famous, there are not larger number of entities in the group, there is no apparent future prospect of the assessee-company, no viable and sentiment creating business is existing or contemplated, there is no apparent justification for charging huge premium, no dividend is paid for a long period, (iv) money is not returned to the lender, no interest or petty interest is charged, there are TDS defaults, (v) there is no apparent known relationship between lender/investor with the assessee which would inspire personal confidence and faith between lender and borrower, when borrower is an individual or a private limited company, (vi) there are instances of cash deposit in the account of lender/investor and thereafter transaction is done with assessee and there is no acceptable explanation about the source of cash, (vii) where directors/shareholders of lender/investor companies are persons of petty means such as chowkidars, peons, drivers who are not expected to run a company of that magnitude. When any of the above factors exist, it is inferred by the AO that it is not probable that a genuine transaction as claimed by the assessee has taken place, because under normal circumstances nobody would invest or lend if any of the above factors exist. Thus, even in those cases where identity and creditworthiness of the creditor/investor is proved, it cannot be said that genuineness of the transaction is proved.

Authorities in support of human probabilities

- There are several instances where Courts have considered certain transactions as not genuine in the light of human probabilities by holding that such transactions in normal circumstances could not have taken place. Some of these authorities have been referred to by the Hon'ble Apex Court in NRA Iron & Steel (P.) Ltd. (supra) as under -

  (i) In Sumati Dayal v. CIT [1995] 214 ITR 801/80 Taxman 89 (SC)

  (ii) In CIT v. P. Mohankala [2007] 161 Taxman 169/291 ITR 278 (SC).

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- (iii) The Delhi High Court in a recent judgment delivered in NDR Promoters Pvt. Ltd. (supra) upheld the additions made by the Assessing Officer. It was found that five companies from whom it received premium were operated by one, 'TG', (Tarun Goyal) Chartered Accountant who had set-up about 90 companies for providing accommodation entries. The assessee had failed to produce directors of shareholder companies, though directors had filed confirmations and, therefore, were in touch with assessee. It was found that directors of all those five companies were either employees of 'TG' or close relatives. They were working as peons, receptionists, etc. The statement of those directors/employees were recorded which revealed that they signed on the papers produced before them by Sh Tarun Goyal. They did not know about the basic details of the companies like shareholding patterns, nature of business of these companies, etc. All five shareholder companies were located at a common address. During search on premises of 'TG', it was found that all passbooks, cheque books, PAN Cards, etc., belonging to said companies were in possession of 'TG'. It was found that 'TG' was appearing in all the income-tax proceedings on behalf of all the investor companies. He was not charging any fees. It was held that the transactions in question were clearly sham and make-believe with excellent paper work to camouflage their bogus nature. The Tribunal ignored evidence and material referred to in the assessment order. The reasoning given by the Tribunal was contrary to human probabilities, for in the normal course of conduct, no one will make investment of such huge amounts without being concerned about the return and safety of such investment.
- (iv) In a recent judgment the Delhi High Court [CIT v. N.R. Portfolio (P.) Ltd. [2014] 42 taxmann.com 339/222 Taxman 157 (Mag.) (Delhi)] held that the credit worthiness or genuineness of a transaction regarding share application money depends on whether the two parties are related or known to each other, or mode by which parties approached each other, whether the transaction is entered into through written documentation to protect investment, whether the investor was an angel investor, the quantum of money invested, credit-worthiness of the recipient, object and purpose for which payment/investment was made, etc. The incorporation of a company, and payment by banking channel, etc., cannot in all cases tantamount to satisfactory discharge of onus.

RECENT SUPREME COURT RULING

- A new Supreme Court ruling has sent shivers down the spine of assesses, because they have to give full information about investors. On being unable to give information, the dangerous Section 68 would be unleashed, with the firm being taxed, right and left. Till now, the angel tax was swooping down upon taxpayers, flapping it's wings but now the devil tax, shaking it's horns, threatens to descend on every assessee.
- **Case of Principal Commissioner of Income-tax v. NRA Iron & Steel (P.) Ltd. - Pr. CIT v. NRA Iron & Steel (P.) Ltd. [2019] 412 itr 161 sc (SC)**
  - The addition u/s. 68, of cash credit, being share capital and premium received by an assessee, has been a contentious issue between taxpayers and the Department. The decision, whether to uphold addition, largely depends upon whether assessee has been able to discharge the onus lying on him with respect to identity of the investor companies, their creditworthiness and genuineness of the transaction? The addition has been deleted either on technical grounds or on facts, if it is found that AO has not carried out required investigation to discharge the onus shifted on him in cases where assessee has submitted all the necessary documentation and discharged the onus lying on him u/s. 68. On the other hand, the addition has been confirmed, wherever it is held on facts that the assessee has not been able to discharge the onus. Such situation arises where AO carries out investigation and prime facie holds that the receipt of share capital and premium is not genuine. The present case namely, Pr. CIT v. NRA Iron & Steel (P.) Ltd. [2019] 103 taxmann.com 48 (SC) falls in this category. The facts of the case, the arguments of the Department and reasoning given by the Hon'ble Apex Court while upholding order of AO, reversing the decision of CIT(A), ITAT and High Court which had decided in favour of assessee, are briefly described below.

Facts of the Case

- The Assessee-Company in it's Income-tax Return showed that money aggregating to Rs. 17,60,00,000/-had been received through Share Capital/Premium, during the Financial Year 2009-10 from 20 companies situated at Mumbai, Kolkata, and Guwahati. The issue before the AO was whether the amount of Rs. 17,60,00,000/-allegedly raised by the Respondent through share capital/premium were genuine transactions or not? The Assessee, inter alia, submitted that the entire Share Capital had been received through normal banking channels by account-payee cheques/demand drafts, and produced documents such as income-tax return acknowledgments to establish the identity and genuineness of the transaction. It was submitted that, there was no cause to take recourse to Section 68 of the Act, and that the onus on the Assessee Company stood fully discharged.
- The AO had issued summons to the representatives of the investor-companies. Despite the summons having been served, nobody appeared. The Department only received submissions through dak, which created a doubt about the identity of investor-companies. The AO independently got field enquiries conducted at Mumbai, Kolkata, and Guwahat. The enquiries at Mumbai revealed that out of the four companies, two companies were found to be non-existent at the address furnished. Regarding Kolkata companies, the response came through dak only. However, nobody appeared, nor did they produce their bank statements to substantiate the source of the funds from which the alleged investments were made. With respect to the Guwahati companies – Ispat Sheet Ltd. and Novelty Traders Ltd., enquiries revealed that they were non-existent at the given address. The A.O. also found that none of the investor-companies which had invested amounts ranging between Rs. 90,00,000 and Rs. 95,00,000 as share capital could justify making investment at such a high premium of Rs. 190 for each share, when the face value of the shares was only Rs. 10; In addition, the companies were declaring a very meagre income in their returns. The Assessee filed an Appeal before the CIT (Appeals) and placed reliance on the decision of the Delhi High Court in CIT v. Lovely Exports Pvt. Ltd. [2008] 299 ITR 268 (SC) case.

Facts of the Case- Cont….

- The ld. AO made the addition of Rs. 17.60 crores after carrying out various inquiries as under-

  (i) Notices were served on three investor-companies, (Clifton Securities Pvt. Ltd.-Mumbai, Lexus Infotech Ltd.-Mumbai, Nicco Securities Pvt. Ltd. Mumbai) but no reply was received.

  (ii) Address was incorrect (Real Gold Trading Co. Pvt. Ltd.-Mumbai)

  (iii) Notice could not be served on two investor-companies (Hema Trading Co. Pvt. Ltd.-Mumbai, Eternity Multi Trade Pvt. Ltd.-Mumbai)

  (iv) Submissions from nine companies were received (Neha Cassetes Pvt. Ltd.-Kolkata, Warner Multimedia Ltd. Kolkata, Gopikar Supply Pvt. Ltd. Kolkata, Gromore Fund Management Ltd. Kolkata, Bayanwala Brothers Pvt. Ltd. Kolkata, Shivlaxmi Export Ltd. Kolkata, Natraj Vinimay Pvt. Ltd. Kolkata, Neelkanth Commodities Pvt. Ltd. Kolkata, Prominent Vyappar Pvt. Ltd. Kolkata), however, they had not given any reasons for paying huge premium. Further, they had very low returned income.

  (v) The details of share purchased and amount of premium not specified by following companies, t hey had not enclosed bank statement (Super Finance Ltd. Kolkata, Ganga Builders Ltd. Kolkata)

  (vi) In addition to above, ld. AO found that:

  - ♦ out of the four companies at Mumbai, two companies were found to be non-existent at the address furnished.
  - ♦ With respect to the Kolkata companies, nobody appeared nor did they produce their bank statements to substantiate the alleged investments.
  - ♦ Guwahati companies - Ispat Sheet Ltd. and Novelty Traders Ltd., were found non-existent at the given address.
  - ♦ None of the investor-companies appeared before the A.O.

Facts of the Case- Cont….

- **Decision by CIT(A):**
  - The ld. CIT(A) on an appeal filed by the assessee deleted the addition following the decision of the Hon'ble Delhi High Court in CIT v. Lovely Exports Pvt. Ltd. [2007] 158 Taxman 440/[2008] 299 ITR 268 holding that assessee had discharged the onus by filing confirmations from the investor companies, their Income-tax Returns, acknowledgements with PAN, copies of their bank accounts to show that the entire amount had been paid through normal banking channels.
- **Decision by the Tribunal:**
  - Appeal filed by the Revenue was dismissed by the Tribunal by holding that Assessee had discharged his primary onus to establish the identity and credit-worthiness of the investors, especially when the investor companies had filed their returns and were being assessed. [refer- ACIT v. NRA Iron & Steel Pvt. Ltd. [IT Appeal No. 3611 (Delhi) 2014, dated 16-10-2017].
- **Decision by the High Court:**
  - TheHon'ble Delhi High Court in Pr. CIT v. NRA Iron & Steel Pvt. Ltd. [IT Appeal No. 244 of 2018, dated 26-2-2018] dismissed the appeal of the Revenue on the ground that the issues raised before it were urged on facts and the lower appellate authorities had taken sufficient care to consider the relevant circumstances. Hence, no substantial question of law arose for their consideration.
- **Arguments of the Department:**
  - It appears that arguments offered by the Department were considered in the reasoning given by the Hon'ble Apex Court for sustaining the order of AO.
- **Arguments of the assessee:**
  - The assessee was not represented by anyone either before the High Court or before the Hon'ble Supreme Court and, hence, the Hon'ble Supreme Court decided the issue ex-parte.

Specific findings of Supreme Court

- The Court in the facts of the case held that explanation should be given in respect of high premium. This fact of high premium per se cannot be a factor to make an addition u/s 68 of the Act, if the other three ingredients are well established. The section merely requires nature and source to be explained. For this very reason, section 56(2)(viib) was inserted in the statute book, wherein excess share premium received over the fair market value can be taxed. In this regard, one can refer to the judgment of the Hon'ble Madhya Pradesh High Court in case of PCIT vs. Chain House International (P.) Ltd. – [2018] 98 taxmann.com 47 (MP), wherein it has been held that once genuineness, creditworthiness and identity of investors are established, no addition can be made only on ground that shares were issued at excess premium. In fact, SLP filed against the said judgment has been dismissed by the very same bench of the Apex Court [SLP(Civil) Diary No(s). 1992/2019]..
- The Court also held that the investor companies did not produce their bank statement to explain their source of funds. This requirement of explaining the source of funds was justified in the facts of the case before the Court because of meagre income shown by investors for the relevant years.

Specific findings of Supreme Court-Cont…

- However, once the creditworthiness is satisfied, there is no requirement for a person to prove the source of source. Secondly, such requirement now finds a specific mention in the statute book in the form of Proviso to section 68 which has come into effect from 1.4.2013. The Hon'ble Bombay High Court in case of CIT vs. Gagandeep Infrastructure Pvt. Ltd.- 394 ITR 680(Bom), has held that such proviso is prospective in nature. Thus, prior to the said date, there cannot be any requirement on the assessee to prove the source of source.
- Of course, this would not prohibit the AO to enquire into the source of source. But then the question would be, if the investor is not able to explain his source, should the additions be made in the hands of the investors or in the hands of the company. One can argue that if the investor company fails to offer any explanation about the source of their funds for investment, the addition should be made in the hands of the investor company and not the assessee company.
- This is because, the wording used in section 68 are "the sum so credited may be charged to tax as the income of the assessee". The section is worded in such a manner so as to give discretionary power to the AO to make addition unlike section 56(2)(x) wherein the difference is automatically considered the income of the assessee. Thus, the option is with the AO to tax it in the hands of the assessee and that he can exercise his discretion to tax it in the hand of the investor.

Specific findings of Supreme Court-Cont…

- However, post insertion of the proviso to section 68 i.e. w.e.f. 1.4.2013, if the investor fails to offer the explanation of source of their investment then addition has to be made in the hands of the assessee-company.
- The Court in the discussed case referred to the meager income of the investor companies to hold that creditworthiness was not proved. This may be because, the other details like the availability of funds in other form or past profits may not be available with the Court. This inference can also be drawn because the Court also held that the investor companies did not demonstrate the source of funds for investment. Thus, merely because in the year in which shares are subscribed, the investor company has earned meager income or suffered a loss would not mean that the investor company has no creditworthiness. If the investor company is able to demonstrate from the balance sheet that it had sufficient funds available with it to invest, then creditworthiness can be said to have been established. The Hon'ble Delhi High Court in case of CIT vs. Ms. Mayawati – 338 ITR 0563(Del) has held that the capacity of any person does not mean how much they earn monthly or annually, but the term capacity has wide meaning and the same can be perceived by how wealthy a person is.
- In so far as the identity aspect is concerned, the Court held that in case of some parties, they were found to be non-existent at the address already furnished. This would lead to the conclusion that the identity is not established. Thus, the traditional concept of giving name, PAN and address has been enlarged to this effect. However, if the person bring confirmation, gives new address and the investor party replies to the summons of the AO, then one can say, in my opinion, that the identity has been established.

Specific findings of Supreme Court-Cont…

- It is important to note that the said judgment of the Court was considered by the Kolkata Bench of ITAT in case of M/s Baba Bhootnath Trade & Commerce Ltd. vs. ITO (ITA No. 1494/Kol/2017). In the said judgment, the Tribunal has distinguished the judgment in case of NRA Iron and Steel (supra) on similar grounds that the facts of the case were different as compared to the facts in the case before the Apex Court. The Tribunal distinguished the judgment of the Apex Court on the following counts:
  - a. the AO in the case before the Apex Court had made extensive enquiries and from that he had found that some of the investor companies were non-existent which was not the case before the Tribunal.
  - b. In the case before the Apex Court, certain investor companies did not produce their bank statements proving the source for making investments in Assessee Company, which was not the case before the Tribunal. In the case before the Tribunal, the entire details of source of source were duly furnished by all the respective share subscribing companies before the AO in response to summons u/s 131 of the Act by complying with the personal appearance of directors.
- From the above discussion, it can be noted that the specific findings of the Court cannot be isolated from other specific findings of the Court to make addition in a particular case. As already specified earlier, the findings of the Court have to be read in the context of the case and not otherwise. In the context of the impugned case, the specific findings are supported by other specific findings which cumulatively lead the Court to give the said judgment.

Specific findings of Supreme Court-Cont…

- It is interesting to note that the Tribunal in the case of NRA Iron and Steel Pvt. Ltd. (ITA.No.3611/Del./2014), while deciding in favour of the assessee had relied upon judgment of the co-ordinate bench of the Tribunal – [ACIT vs. M/s. Adamine Construction Pvt. Ltd. -ITA No. 6175/Del/2013] wherein identical issues were involved, in fact, few of the investor companies were also common. In the case of the said company i.e. M/s. Adamine Construction Pvt. Ltd., the matter travelled upto the Hon'ble Supreme Court and in that case, the Court had dismissed the SLP of the Department [PCIT v. Adamine Construction (P.) Ltd. (2018) 259 Taxman 131 (SC)]. Ironically, one of the judges in both the cases is common.

Analysis

- The Hon'ble Apex Court in case of CIT vs. Sun Engineering Works (P) Ltd. –(1992) 198 ITR 0297 (SC) has held that "The judgment must be read as a whole and the observations from the judgment have to be considered in the light of the questions which were before this Court. A decision of this Court takes its colour from the questions involved in the case in which it is rendered and, while applying the decision to a later case, the Courts must carefully try to ascertain the true principle laid down by the decision of this Court and not to pick out words or sentences from the judgment, divorced from the context of the questions under consideration by this Court, to support their reasoning."
- Similarly, the judgment of the Court as rendered in the impugned case, has to be considered in the light of the facts existing in the case. The Court itself, in para 15, states that in the facts of the present case, the assessee company failed to discharge the onus laid down u/s 68 of the Act.
- Also, it is well known that the additions made u/s 68 of the Act are fact specific. It depends upon the details and evidences produced by the assessee to discharge the initial onus and the inquiry and investigation of the AO in the course of assessment proceedings. Thus, carte blanche application of the present judgment to all the cases involving addition of share capital etc. u/s 68 of the Act would not be justified.
- Nevertheless, the Court has laid down some important ratios which would be applicable to similar cases.

Supreme Court's Ruling

- The Supreme Court heard the matter on 5-2-2019 and pronounced that the issue which arose for determination was whether the Assessee had discharged the primary onus to establish the genuineness of the transaction required under Section 68 of the Act. As per settled law, the initial onus was on the Assessee to establish by cogent evidence the genuineness of the transaction, and credit-worthiness of the investors under Section 68 of the Act. The assessee was expected to establish to the satisfaction of the Assessing Officer as specified in [CIT v. Precision Finance (P.) Ltd. [1994] 208 ITR 465/[1995] 82 Taxman 31 (Cal)].
- **Reasoning given by the Hon'ble Supreme Court:**
  - (i) There was no material on record to prove, or even remotely suggest, that the share application money was received from independent legal entities. The survey revealed that some of the investor companies were non-existent and had no office at the address mentioned by the assessee. The onus to establish the identity of the investor companies, was not discharged by the assessee.
  - (ii) The enquiries revealed that the investor companies had filed returns for a negligible taxable income, which would show that the investors did not have the financial capacity to invest funds ranging between Rs. 90,00,000 to Rs. 95,00,000 in the Assessment Year 2009-10, for purchase of shares at such a high premium. The investor-companies which had filed income-tax returns with a meagre or nil income had to explain how they had invested such huge sums of money in the Assessee-Company.

Supreme Court's Ruling-Cont…

- (iii) There was no explanation whatsoever offered as to why the investor companies had applied for shares of the Assessee-Company at a high premium of Rs. 190 per share, even though the face value was Rs. 10 per share.
- (iv) Furthermore, none of the so-called investor-companies established the source of funds from which the high share premium was invested.
- (v) The mere mention of the income-tax file number of an investor was not sufficient to discharge the onus under Section 68 of the Act.
- (vi) In the case of private placement of shares, a higher onus is required to be placed on the Assessee since the information is within the personal knowledge of the Assessee. The Assessee is under a legal obligation to prove the receipt of share capital/premium to the satisfaction of the AO.

It was held the by the Hon'ble Apex Court, on the facts of the present case, the Assessee-Company failed to discharge the onus required under Section 68 of the Act. Therefore, the Assessing Officer was justified in adding back the amounts to the Assessee's income.

Comments of Supreme Court

I. Proof of Identity of the creditors; Capacity of creditors to advance money.

(1) Identity of the investor companies - It is proved by Certificate of incorporation, the existence of directors and their DIN issued by MCA. The data from MCA/ ROC portal showing the registration of the company, its compliance of the requirements of ROC, various documents filed by the investor companies with ROC, its continuity of existence since the year of investment till the date of assessment of assessee-company and thereafter, fact of not delisting of investor company, assessment orders (particularly scrutiny assessments, where notices u/s. 143(2) are served on the investor companies and representation/compliance is made by them before their AO) of the relevant year and of subsequent years of the investor companies, any legal proceeding against the investor companies under any other law where existence of investor companies is apparently visible. Further, where an investor company is accepted as existing by the Department for the purposes of recovering taxes from it, they should not disbelieve the existence of such company for the purposes of investment made by it. PAN or acknowledgement of return are prima facie evidences which are countered by the AO by finding that investor companies do not exist at the given address. For office address the photo with signboard of investor companies should be provided. These days there is a requirement of ROC to file online a photo of the signboard of the company with director standing against it and photo of the director sitting in his chamber. Such evidence will be useful for establishing identity of the investor-company and its independent legal existence. The fact that investor company is not removed from the roaster of ROC will also help in acceptance of existence.

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- CIT v. Dwarkadish Investment [2010] 194 Taxman 43/[2011] 330 ITR 298 (Delhi)--It was held "In any matter, the onus of proof is not a static one. Though in Section 68 the Income-tax Act, 1961, the initial burden of proof lies on the assesses, yet once he proves the identity of the creditors/share applicants by either furnishing their PAN number or income-tax assessment number and shows the genuineness of transaction by showing money in his books either by account-payee cheque or by draft or by any other mode, then the onus of proof would shift to the Revenue. Just because the creditors/share applicants could not be found at the address given, it would not give the Revenue the right to invoke Section 68. One must not lose sight of the fact that it is the Revenue which has all the powers and wherewithal to trace any person.-
- CIT v. Divine Leasing & Finance Ltd. [2007] 158 Taxman 440/[2008] 299 ITR 268 (Delhi)--The Delhi High Court held that the amount of share application money received by a company from alleged bogus share holders could not be regarded as undisclosed income u/s 68 when the assessee furnished details regarding shareholders. If the names of the alleged bogus shareholders are given to the AO, then the department is free to proceed to reopen their individual assessments in accordance with law. The assessee can't be expected to know every detail pertaining to identity and financial worth of each of it's investors …burden of proof can't be discharged to the hilt if AO harbours some suspicion."
- CIT v. STL Extrusion (P.) Ltd. [2011] 11 taxmann.com 125/333 ITR 269 (MP)--Where assessee had duly discharged its onus by furnishing names, age, address, date of filing application of share, number of shares of each subscriber, the AO was not justified in making addition u/s 68 of Act.
- CIT v. Creative World Telefilms Ltd. [2011] 15 taxmann.com 183/203 Taxman 36 (Bom.) (Mag.)--Once documents like PAN card, bank account details or details from the bankers were given by the assessee, onus shifted upon the Assessing Officer and it was on him to reach the shareholders. The Assessing Officer could not burden the assessee merely on the ground that summons issued to the investors were returned back with the endorsement not traceable

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- CIT v. Orchid Industries [2017] 397 ITR 136/397 ITR 136 (Bom.)--The summons could not be served as some of investors were not traced. The profit and loss account showed that sufficient funds existed. The Bombay High Court held that just because sum could not be traced, the amount could not be taxed under Section 68 in assessee's hands.
- Madhuri Investments v. ACIT [IT Appeal No. 110 of 2004] Karnataka--The company does not identify where applicants are genuine or their addresses are correct, while inviting share applications. As the notices came back with 'no such person' written, one could not call them bogus. For some reason, the address might have changed, or the summons were not received or incorrect address in application might have been given.
- Umbrella Projects v. ITO (IT Appeal No. 5955 (Delhi) of 2014]--Out of 19 investors, if 4 were not found, the assessee could't be brought within the mischief of Section 68, the ruling held.
- Ashtech Industries v. Dy. CIT [IT Appeal No. 2332 (Delhi) of 2008]--The non-production of directors doesn't mean Section 68 additions can be made.
- CIT v. Jalan Hard Coke [2018] (95 taxmann.com 331/257 Taxman 91 (SC)--In this Supreme Court's decision it was held that no addition under Section 68 could be made if assessee failed to produce shareholder applicants. It also said that one could not assess to tax to find out who applied as shareholder.

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(2) Where notices on investor companies are not served: This may be possible due to change of addresses of the investor companies. The assessee is expected to provide the latest address of the investor companies.

(3) Where investor companies are summoned to appear: Where the AO issues summons to the old directors (the directors who were on the record in the relevant assessment year) then action of the AO may not be held correct as old directors are not bound to appear as they no longer hold the post. Under this situation the assessee may inform the AO the identity of the present directors or the AO can find out the same from MCA portal. Further, where the directors do not intend to appear in response to summons, it is their duty to provide adequate reasons for non-appearance. In any case, non-appearance of the directors before the AO should not go against the assessee as held in CIT v. Orchid Industries (P.) Ltd. [2017] 88 taxmann.com 502/397 ITR 136 (Bombay).

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(4) About creditworthiness of the investor companies: Merely investor companies having low income should not be treated as lack of creditworthiness. Here the assessee is required to provide the balance sheet of investor companies for atleast three years including the relevant year and if available on MCA portal and balance sheet of latest year to show/identify (i) share capital, (ii) Reserves and surplus, (iii) Long-term investments, (iv) total assets, (v) cash and cash equivalent. Creditworthiness depends upon capacity and wealth of the investor and not merely on low income. Low income may create doubt, but this can be dispelled with huge assets and investments already in the balance sheet of the investor company. Further, it has been held in CIT v. Value Capital Services (P.) Ltd. [2008] 307 ITR 334 (Delhi) (HC); Prabhatam Investment (P.) Ltd. v. ACIT IT Appeal Nos. 2523 to 2525/Del./2015, dated 17-4-2017]; CIT v. Vrindavan Farms (P.) Ltd. etc., [IT Appeal No. 71 of 2015, dated 12-8-2015], that low income of the investor companies may not be sufficient to hold that investor companies do not have creditworthiness. Further, for proving creditworthiness, the bank statement of the investor companies should be submitted so as to show that they had adequate funds at their disposal in the bank account for making investment in assessee-company. Source of immediate credit in the bank account of investing company for making investment is also required to be explained after 1-4-2013.

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- This Court in the landmark case of Roshan Di Hatti v. CIT [1977] 107 ITR 938 (SC) laid down that the onus of proving the source of a sum of money found to have been received by an assessee, was on the assessee. Once the assessee had submitted the documents relating to identity, genuineness of the transaction, and credit-worthiness, then the AO had to conduct an inquiry, and call for more details before invoking Section 68. If the Assessee was not able to provide a satisfactory explanation of the nature and source, of the investments made, it was open to the Revenue to hold that it was the income of the assessee, and there would be no further burden on the revenue to show that the income was from any particular source. With respect to the issue of genuineness of transaction, it was for the assessee to prove, that the investments made in share capital were genuine borrowings, since the facts were exclusively within the assessee's knowledge. Reliance was also placed on the decision of CIT v. Kamdhenu Steel & Alloys Ltd. [2012] 19 taxmann.com 26/206 Taxman 254/[2014] 361 ITR 220 (Delhi) wherein the Court held that :"It is projected by the Revenue that the Directorate of Income-tax (Investigation) had purportedly found a racket of floating bogus companies with sole purpose of lending entries. But, it was unfortunate that all this exercise was going in vain as few more steps by the Revenue in order to find out causal connection between the case deposited in the bank accounts of the applicant banks and the assessee were not taken. It was necessary to link the assessee with the source; when that link was missing, it was difficult to fasten the assessee with such a liability."

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- CIT v. Arunananda textiles (P.) Ltd. [2011] 15 taxmann.com 226/203 Taxman 32 (Mag.)/333 ITR 116 (Ker.)--It was not for the assessee to place material before the Assessing officer about creditworthiness of the shareholders. The PAN had been given. Once the company had given the addresses of the shareholders and their identity was not in dispute, it was for the Assessing Officer to make further inquiry with the investors about their capacity to invest the amount in shares.

- CIT v. Value Capital Services [2008] 307 ITR 334 (Delhi)--The Delhi High Court ruled that even if investor does not have means, the Revenue has to prove that the amount emanated from assessee's coffers.

Comments of Supreme Court-Cont…

II. Genuineness of Transactions

On the issue of unexplained credit entries /share capital, the Court examined the following judgments

- In a recent judgment the Delhi High Court [CIT v. N.R. Portfolio (P.) Ltd. [2014] 42 taxmann.com 339/222 Taxman 157 (Mag.)] held that the credit-worthiness or genuineness of a transaction regarding share application money depends on whether the two parties are related or known to each other, or mode by which parties approached each other, whether the transaction is entered into through written documentation to protect investment, whether the investor was an angel investor, the quantum of money invested, credit-worthiness of the recipient, object and purpose for which payment/investment was made, etc. The incorporation of a company, and payment by banking channel, etc., cannot in all cases tantamount to satisfactory discharge of onus.
- Is the transaction real or fake, that's the question which agitates the tax officer. Though the process has taken place through bank, the raising of such a query is astonishing. The AO should ask the concerned AO of investor/creditor regarding genuineness of transaction. Dataware (P.) Ltd. v. CIT [IT Appeal No. 263(Calcutta) of 2011]

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- In the present case, the A.O. had conducted detailed enquiry which revealed that :
  i. There was no material on record to prove, or even remotely suggest, that the share application money was received from independent legal entities. The survey revealed that some of the investor companies were non-existent, and had no office at the address mentioned by the assessee. For example, companies Hema Trading Co. Pvt. Ltd. and Eternity Multi Trade Pvt. Ltd. at Mumbai, were found to be non-existent at the address given, and the premises was owned by some other person. The companies at Kolkata did not appear before the A.O., nor did they produce bank statements to substantiate the source of funds. The two companies at Guwahati, viz., Ispat Sheet Ltd. and Novelty Traders Ltd., were found to be non-existent at the address provided. The genuineness of the transaction was found to be completely doubtful.
  ii. The enquiries revealed that the investor-companies had filed returns for a negligible taxable income, which would show that the investors did not have the financial capacity to invest funds ranging between Rs. 90,00,000 to Rs. 95,00,000, for purchase of shares at such a high premium. For example, Neha Cassettes Pvt. Ltd. - Kolkata had disclosed a taxable income of Rs. 9,744/- , but had purchased Shares worth Rs. 90,00,000 in the Assessee-Company. Warner Multimedia Ltd. – Kolkata filed a NIL return, but had purchased Shares worth Rs. 95,00,000 in the Assessee-Company. Ganga Builders Ltd. – Kolkata filed a return for Rs. 5,850 but invested in shares to the tune of Rs. 90,00,000 in the Assessee-Company. The lower appellate authorities appeared to have ignored the detailed findings of the AO from the field enquiry and investigations carried out by his office. They failed to appreciate that the investor-companies which had filed income-tax returns with a meagre or nil income had to explain how they had invested such huge sums of money in the Assessee-Company. The entire transaction seemed bogus, and lacked credibility.

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- The practice of conversion of un-accounted money through the cloak of Share Capital/Premium must be subjected to careful scrutiny. This would be particularly so in the case of private placement of shares, where a higher onus is required to be placed on the Assessee since the information is within the personal knowledge of the Assessee. The Assessee is under a legal obligation to prove the receipt of share capital/premium to the satisfaction of the AO, failure of which, would justify addition of the said amount to the income of Assessee. On the facts of the present case, clearly the Assessee-Company failed to discharge the onus required under Section 68 of the Act and the Assessing Officer was justified in adding back the amounts to the Assessee's income. The Appeal filed by Revenue was allowed. In the aforesaid facts and circumstances, and the law laid down above, the judgment of the High Court, the ITAT, and the CIT were thereby set-aside. The Order passed by the AO was restored.
- This element assumes importance to decide about genuineness of the transactions. In the eyes of the AO, where investor companies do not justify payment of huge premium, the transaction would appear to be non-genuine. Since u/s. 68 it is the subjective satisfaction of the AO, though should have been taken objectively, but an onus is cast on the assessee to justify why the investor companies have agreed to pay huge premium. In this regard, one may refer to the judgments in Green Infra Ltd. v. ITO [2013] 38 taxmann.com 253/145 ITD 240 (Mum. - Trib.) which is confirmed by the Hon'ble Bombay High Court in CIT v. Green Infra Ltd. [2017] 78 taxmann.com 340/392 ITR 7, where it is held that it is a prerogative of the Board of Directors of a company to decide the premium amount and it is the wisdom of the shareholders whether they want to subscribe to such a heavy premium? However, it would be a prudent exercise on the part of the assessee to justify charging of huge premium on the basis of goodwill of the group, potential activities of the assessee-company and estimated growth in NPS.

Comments of Supreme Court-Cont…

III. Whether evidences collected by the AO are confronted to the assessee?

- Where assessee discharges primary onus cast on him u/s. 68, the AO carries out inquiries and investigation in respect of identity and creditworthiness of the investor companies and genuineness of transaction. It is incumbent on him to confront to the assessee the evidence collected by him. In the present case, decided ex-parte by the Hon'ble Apex Court, it does not appear that assessee was confronted by the AO with those evidences which created doubt over identity, creditworthiness of the investor companies and genuineness of transaction of investment. Thus, it appears that this important aspect was not considered by the AO and apparently not argued by the assessee and, therefore, was not considered by the Hon'ble Supreme Court in the present case.
- In this regard, one may refer to following judgments- Andaman Timber Industries v. CCE [2015] 62 taxmann.com 3/52 GST 355 (SC); Kishinchand Chellaram v. CIT [1980] 4 Taxman 29 (SC); Prinku landfin (P.) Ltd. v. ITO [2018] 91 taxmann.com 120/170 ITD 139 (Delhi - Trib.); Premier Electrical Industries v. Jt. CIT [2016] 76 taxmann.com 14/[2017] 162 ITD 45 (Chd. - Trib.); Inder Singla v. ITO [2017] 82 taxmann.com 74 (Chd. - Trib.); Alok Agarwal v. Dy. CIT [2000] 67 TTJ 109 (Delhi); Smt. Madhu Killa v. Asstt. CIT [2018] 100 taxmann.com 264 (Kol. - Trib.); Bioved Research Society v. CIT [2018] 91 taxmann.com 268/170 ITD 160 (All.-Trib.).
- Therefore, wherever AO collects evidence against the assessee and does not confront the same to him before using it against him, the addition cannot be sustained. This legal requirement is relevant for distinguishing the present case. One may obtain the order of the AO in NRA Iron & Steel (P.) Ltd. and examine whether principles of natural justice were followed or not.

Comments of Supreme Court-Cont…

IV. Why Company Must be Spared

- Technically, the income-tax department has the vast machinery and resources to find out about investors, if it wills. Instead, the new ruling means that the company would have to carry the burden. There are three points, namely, identity and creditworthiness of investors and genuineness of transaction which have to be wholly proved by the assessee-company, which is simply shocking.

V. Source of Source Can't be Inquired

- It is nowhere stipulated that the assessee-company has to examine source of source of funds. That is, how the investor got the money is beyond the pale of company's investigation. For example, in CIT v. K.C. Fibres [2010] 187 Taxman 53/[2011] 332 ITR 481 (Delhi), it was categorically held that, "It is not for assessee-company to prove where investor got money."

VI. Why High Premium is Not Questionable

- Why investors went in for shares with high premiums is a pet question that is asked by income-tax authorities. It is an inane query. In CIT v. Green Infra Ltd. [2017] 78 taxmann.com 340/392 ITR 7 (Bom.) case, the Bombay High Court held that it is the prerogative of Board of Directors to decide premium amount and the wisdom of shareholders whether they want to subscribe to such a heavy price.

Comments of Supreme Court-Cont…

VII. Section 133(6) of Act.

- Through PAN, the tax official can get the income-tax returns of suspected investors and find whether they have sufficient funds

VIII. Various ways in which the tax officer can satisfy curiosity, instead of applying Section 68, the dreaded provision.

- The AO can verify through PAN or bank account if there is no answer to summons.
  - Was any cash deposited in investor's bank account, before issuing cheque ?
  - The AO can also find out whether there was immediate withdrawal from bank by company, before the investor brought in share capital or share premium?
  - AO can find about 'missing' investors through postal department.

IX. Absurd Situations

- In Champaklal Dhamanwala v. ITO [1990] 34 ITD 209 (Ahd.) case, the court had to step in and say that "after 20 years don't expect proof about genuineness of a transaction," protecting the assessee from the mischief of Section 68 of Act. Many times, Section 68 is sought to be imposed for the single reason that all investors had registered office at one address. But there is no bar against operating from one place.
- A wife was an investor in husband's company, but he did not know about it. The tax authorities felt there was collusive arrangement between them and sought to bring in Section 68 of Act. The court ruled in this case [S N Ganguly v. CIT [1953] 24 ITR 16 (Patna)] that husband is not presumed to have prior knowledge, unless the department proves he was aware of the fact.

To what extent this judgment has binding force?

- (i) The judgment is apparently per incuriam of their own judgment in the case of CIT v. Lovely Exports Pvt Ltd. [2008] 216 CTR 195 (SC)] wherein the special leave petition filed by the Department against the order of the Delhi High Court was dismissed with the following remarks:—

  "We find no merit in this Special Leave Petition for the simple reason that if the share application money is received by the Assessee Company from alleged bogus shareholders, whose names are given to the AO, then the Department is free to proceed to reopen their individual assessments in accordance with law. Hence, we find no infirmity with the impugned judgment".

  The above decision of the Hon'ble Supreme Court follows the earlier decision of the Hon'ble Supreme Court in the case of CIT v. Steller Investment Ltd. [2001] 115 Taxman 99/251 ITR 263, in this case the Hon'ble Supreme Court approved of the judgment of the Delhi High Court reported in CIT v. Steller Investment Ltd. [1991] 59 Taxman 568/192 ITR 287, in which it was, inter alia, held as under:

  In the present case, it cannot be said that the Hon'ble Supreme Court had considered its decision in Lovely Exports Pvt. Ltd. (supra) and consciously departed from its ratio. It only considered the decision of the Hon'ble Delhi High Court in Lovely Exports.

To what extent this judgment has binding force?-Cont...

'It is evident that even if it be assumed that the subscribers to the increased share capital were not genuine, nevertheless, under no circumstances can the amount of share capital beregarded as undisclosed income of the assessee. It may be that there are some bogus shareholders in whose names the shares had been issued and money may have been provided by some other persons. If the assessment of the persons who were alleged to have really advanced the money is sought to be reopened, that would have made some sense but we fail to understand as to how this amount of increased share capital could be assessed in the hands of the company itself.' It is held in CIT v. B.R. Constructions [1993] 202 ITR 222/[1994] 73 Taxman 473 (AP) that a precedent ceases to have a binding force when it is rendered per incuriam (decision decided without referring to a statutory provision or a precedent).

- (ii) This decision in NRA Iron & Steel (P.) Ltd. (supra) is decision on facts and is only binding when facts are similar in other cases, otherwise, they are binding on the parties only. It is held in CIT v. Peerless General Finance and Investment Co. Ltd. [2006] 154 Taxman 179/282 ITR 209- [Calcutta High Court] that the binding nature of a decision is of two kinds—one is in relation to the facts and the other is in relation to the principles of law. A principle of law declared would be treated as precedent and binding on all. The finding of facts would bind only the parties to the decision itself and it is the ultimate decision that binds. Where facts are distinguishable, such as assessee has replied and clarified all the doubts like non-service of summons on the directors of the investing companies due to change of address, existence of the investing companies on the portals of MCA/ROC and with the Income Tax Department long after investment, providing DIN of directors of investing companies and their other particulars, providing reasons for charging huge premium, adequate creditworthiness on the basis of assets, source of immediate availability of funds for investment, etc., then this decision in NRA Iron &
- Steel (P.) Ltd. (supra) cannot be applied.

To what extent this judgment has binding force?-Cont...

- (iii) Onus shifted to the assessee must be discharged - Where assessee furnishes all the documents at the first instance such as PAN, certificate of incorporation, confirmations, bank accounts, addresses of the investor companies, the onus is shifted to the AO. Thereafter, where AO carries out inquiries, issues summons to the investor companies and due to non-service or otherwise satisfaction about nature and source of credit (share capital and premium) is not arrived by the AO, then onus is shifted back to the assessee. Under this situation, it is necessary on the part of the assessee to furnish evidence/explanation in respect of the points which create doubts about identity, creditworthiness or genuineness of transactions (of receiving share capital and premium). As suggested above, various documents in respect of all the three ingredients must be furnished at this stage and genuine efforts to produce the directors of investing companies must be shown, such as writing letters, phone calls, e-mails, etc. A counter-request to the AO to exercise his power to enforce attendance of directors should be made. The ratio of this decision would be applicable when assessee fails to discharge to onus falling on it in the second round.

A Shell-Shocker of a Judgment

- An income-tax officer asked a company head: "How many of your investors wear costly rings on all their fingers?" The distraught assessee said; "How can I know, sir?" The tax official continued: "How many have lunch in Mumbai and breakfast in London ?" The panicky assessee said: "I really cannot say, sir." The income-tax officer asked; "How many of your investors have a rich father-in-law?" The flabbergasted assessee looked heaven wards. The intention of income-tax department in Pr. CIT v. NRA Iron & Steel Co. [2010] 103 taxmann.com 48 (SC) case was to catch shell companies, but it has, in fact, left shell-shocked the common assessee. The judgement's sinister implications are: (a) all companies would be covered under Section 68 and required to furnish evidence about investors, (b) primary evidence would not be enough, full evidence has to be furnished.

Overturns Previous Supreme Court Judgments

- The NRA Iron & Steel case has gone against many Supreme Court's rulings of the past:

(i) CIT v. Lovely Exports Pvt. Ltd. (supra)

The assessee-company had furnished the necessary details such as PAN No., Income-tax ward no., ration card of the share applicants and some of them were assessed to tax. The monies were received through banking channels. In some case's, affidavits/confirmations of the share applicants containing the above information were filed. It was held that all such details constitute acceptable proof or acceptable explanation. The Department would not be justified in drawing an adverse inference only because the creditor/subscriber fails or neglects to respond to its notice; If the share application money is received by the assessee-company from alleged bogus shareholders, whose names are given to the AO, then the Department is free to proceed to reopen their individual cases. It was also held that even if the share capital was bogus the addition should be made in the hands of share applicants and not the assessee-company

Overturns Previous Supreme Court Judgments-Cont..

(ii) CIT v. Steller Investment Ltd. [2001] 115 Taxman 99/251 ITR 263 (SC) :

The apex court held that even if subscribers to the capital are not genuine, the amount received by the company as share capital could not be assessed in the hands of the company itself. Such amounts should be considered for assessment in the hands of persons who are alleged to have really advanced the money.

(iii) CIT v. Orissa Corpn. [1986] 25 Taxman 80 F/159 ITR 78 (SC)

The AO had sent summons to investor but the answer came that the person had 'left.' The Supreme Court held merely because the investor did not appear for summons does not mean that the invested sum was unexplained amount of the assessee.

Concluding Remarks on SC Ruling:

- On 5th March, 2019, The Supreme Court in the case of Principal Commissioner of Income Tax (Central) - 1 Vs. NRA Iron and Steel seems to have disparaged the settled position of law with respect to assessment years prior to Finance Act 2012. In this case, the Department made addition merely on surmises and to that effect the taxpayer discharged its onus by filing Income Tax Returns, Permanent Account Number (PAN), Credits received in the Banks Account, Bank Statements of investor companies. The Commissioner Appeals (First Appellate body) deleted the addition made by the Department stating that the initial onus under section 68 of the Act for establishing the credibility and identity of the shareholders. This view was upheld by the Income Tax Appellate Tribunal (Final Fact-Finding body) as well as the High Court.
- The issue on share capital being alleged as bogus by the Department and thereby addition being made under section 68 of the Income Tax Act, 1961, was settled by the Supreme Court in the case of Lovely Exports 216 CTR 195 more than a decade back!

Concluding Remarks on SC Ruling-Cont…

- Time and again, the Department has tried to nudge this issue before various judicial forums and finally vide the Finance Act 2012, the Income tax Law was amended to curb the menace of several taxpayers converting their undisclosed income by way of subscribing share capital bearing large amount of share premium through dummy / bogus companies as shareholders in a company. However, the amendment clearly prescribes that if the shareholder of the company is able to demonstrate the nature and source of subscribing the share capital in the company and the Department is satisfied by such explanation, then addition shall not be made under section 68 in the hands of the company. In short, if the shareholder is able to demonstrate the genuineness to the satisfaction of the Department, then addition will not be made to the company.
- The Hon'ble Supreme Court reversed the findings of all three bodies i.e. Commissioner Appeals, Income Tax Appellate Tribunal as well as the High Court and confirmed the order of the Assessing Officer.

Concluding Remarks on SC Ruling-Cont…

- With great respect to the Supreme Court there are shortcomings in the judgment passed which are as follows:

1) The Supreme Court has cited the judgment of the Hon'ble Delhi Hight Court in the case of Lovely exports and law established by it which was accepted by the Hon'ble Supreme Court (216 CTR 195 (SC)). The Hon'ble Supreme Court in the said order held,

"Section 68 of the Income-tax Act, 1961 - Cash credit - If share application money is received by assessee-company from alleged bogus shareholders, whose names are given to Assessing Officer, then Department is free to proceed to reopen their individual assessments in accordance with law but this amount of share money cannot be regarded as undisclosed income under section 68 of assessee-company."

2) A new law has been laid down ex-parte, the Hon'ble Supreme Court should have appointed an amicus curiae or lawyer for Respondent before upsetting the finding of crucial authorities that is Commissioner Appeals, Income Tax Appellate Tribunal as well as the High Court.

- With Due respect, if Hon'ble Bench of the Supreme Court wanted to overrule the above position of law they ought to have referred it to Chief justice for constituting a larger bench.

Concluding Remarks on SC Ruling-Cont…

3) With due respect The Hon'ble Supreme Court could not have made the amendment brought by Finance Act, 2012 retrospective without distinguishing the judgment of Hon'ble High Court which have declared it to be prospective.

4) The Bombay High Court in the case of Commissioner of Income Tax-1 V/s. M/s. Gagandeep Infrastructure Pvt. Ltd. (Income Tax Appeal No. 1613 of 2014) rendered on 20th March, 2017 and in The Pr. Commissioner of Income Tax-5 V/S. M/s. SDB Estate Pvt. Ltd. (Income Tax Appeal No. 1356 of 2015)] rendered on 27th March, 2018 has held that the requirement to explain the source of the source of the funds in respect of the investment as shareholders in which the public are not substantially interested as share application money is only prospective as it is introduced w.e.f. 1st April, 2013. This judgement and judgement in the matter of Himachal Fibers Limited ought to have been shown to The Hon'ble Supreme Court by the counsels of department.

Under the circumstances with great respect to the Hon'ble Supreme Court, this judgement should be revisited on the grounds of it being prima facie per incuriam and sub-silentio.

Conclusion

- Angry father once told his son : "I told you to study about our company. You are to soon join the firm. But, I find you reading about our investors." Son replied: "If I don't know about the investors, the income-tax department would study, analyse and dissect us under Section 68, dad."A dreaded provision, Section 68 imposes a super heavy tax of 83.25%, which is frightening. With the new Supreme Court ruling, companies face the daunting task of living fully informed about investors. It is absolutely essential that Section 68 should be modified so that task of finding about investors is performed by the income-tax department. Companies should not be asked to do cop duty. Here's a recent conversation overheard at income-tax office: One income-tax officer asked: "Have you given all information about investors? " The assessee replied: "Yes." The tax official persisted: "Everything???" The assessee said: "Yes, everything." The tax officer again asked: "Has full information been given about each and every investor?" The assessee replied: "Yes, every investor has been covered. I have even given the horoscope of each investor."

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- As per the statutory provision of Sec 68 and jurisprudence of the Hon'ble court, it is clear that primarily the onus is on the assessee to discharge that the credit received by him is from the sources whose identity can be proved, the genesis of the transaction and the creditworthiness of the creditor is proved by documentary evidence. If the assessee presents all these during the assessment proceeding before the AO, the responsibility shifts to the AO to prove it wrong. If AO accepts such evidences without proving it wrong, it can be said that assessee has discharged his onus. If AO presents some contrary evidences, the responsibility again shifts upon the assessee to rebut such contrary evidences.
- The decision of the Hon'ble Apex Court in NRA Iron & Steel (P.) Ltd. (supra) is important as it will enable the AO to curb the practice of obtaining share capital at high premium from unknown parties which create doubt as to their genuineness, particularly when the investor companies are showing very low income, have no known business activities, their offices generally remain in oblivion, their directors are persons of no means and belong to lower strata of society and thereafter there is no gain to the investor companies even after investing such huge sum in the assessee-company. However, this decision is given on facts and cannot create a binding precedence in all fact matrices. One different relevant fact may change the entire complex of the case. Where the AO has not followed the principles of natural justice, has not confronted the assessee the material gathered by him which creates doubt on the explanation submitted by the assessee about nature and source of share capital and premium, or where assessee has submitted adequate evidences clarifying the doubt and suspicion of the AO and there is no further obligation remaining on him, or where AO expects the assessee to discharge an impossible obligation (like not able to produce the directors of the investor companies, inspite of his best efforts), or where the AO does not consider the data downloaded from ROC/MCA portal about existence and continuity of investor companies, the present decision in NRA Iron & Steel (P.) Ltd. (supra) may not be of much help to the Revenue.

CONT…

- Notably, the judgment would cause little impact after 1.4.2013, as the Legislature has already taken required measures vide Finance Act, 2012. The proviso to section 68, is a very strong measure wherein a company is required to even explain the source of the investor, which presupposes the fact that the company would be able to get those evidences easily as the investor would be a known party.

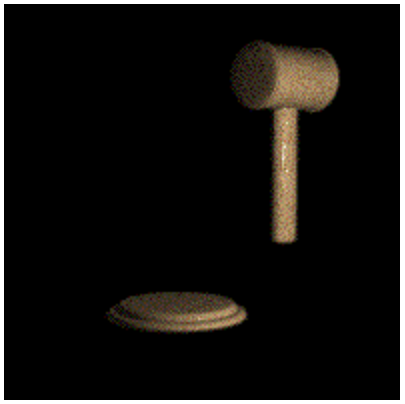
- However, prior to AY 2013-14, i.e. in case of pending disputes pertaining to earlier years, the judgment of the Apex Court so discussed, would have a considerable impact. One has to carefully distinguish the said judgment, so as to reduce it rigours, while applying to the facts of other cases. In any case, there should no longer be any doubt that one has to now furnish a lot details to discharge the onus and one cannot simply wash his hands by furnishing name, address and PAN.

CONT…

- Section 106 of the IE Act is a relevant provision in the context of discharge of burden lying on the assessee u/s. 68. The burden of the assessee u/s. 68 of IT Act is confined to establish, atleast prima facie, the identity and creditworthiness of the creditors and genuineness of transactions which is normally proved by banking transactions if there is no adverse material in the bank account of the lender/investor. Where all the necessary documents to prove three ingredients are submitted, the onus shifts on the Revenue to find holes in the story put up by the assessee. It will not be merely oral assertion by rejecting the explanation submitted by assessee but has to be supported by material evidence. The evidence so collected by the AO, regarding identity and creditworthiness of the lender/investor, has to be confronted to the assessee on whom the onus is now shifted. If the assessee fails to discharge the onus, the amount of credit will be taxed u/s. 68. Where this onus is also discharged then further onus is created on the assessee on account of human probabilities. This is relevant to establish genuineness of transaction. All the factors which led the AO to believe that transaction is not genuine, as based on human probabilities, that such transaction could not have taken place, has to be confronted to the assessee. Again, mere inference/assertion of AO, based on human probabilities will not be enough unless confronted to the assessee. Where Department has carried out searches on entry operators, mere reliance on report of investigation wing is not enough and the burden u/s. 106 of IE Act is on the Revenue to prove the fact that credit entry of the assessee is an accommodation entry on the basis of evidence/statement collected in the search over entry operators.

Issues for consideration

Queries please!?!



Thank you