

# CASH CREDITS – ASSESSMENT OF CONTENTIOUS ISSUES

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## Synopsis:

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## Introduction

**S**ection 68 of the Income Tax Act, 1961...!!, One of the most contentious Sections under the said Act. The Tribunals and Courts have given rich judgments, both in favour of Assessee and the Revenue. In following paragraphs, quoting few words on Cash Credits and contentious issues involved in its assessments.

The Section is meant to curb generation of unaccounted money and it is in clarificatory nature. That means the assessing officer can add a lump sum as of income from undisclosed sources.

Interestingly, there was no corresponding provision in the erstwhile Act, i.e. The Income Tax Act, 1922 and current proviso continued unamended till 1988. A very slight amendment adopted by The Direct Tax Laws (Amendment) Act, 1987 with effect from 01.04.1988. Subsequently, inserted two key provisions vide Finance Act, 2012 (which will be dealt in later part). Further, Section 68 of the present Act is statutorily authorised an Assessing Officer to assess the unexplained cash credit as 'Income and add back to the total income of an assessee accordingly.'

## Objects to adopt for the first time

As a measure to prevent generation and circulation of unaccounted money and clamp the prevailing practices like

1. Concealment of unaccounted cash by showing the same as lent or deposited with them by third parties;
2. Showing of unaccounted cash as their own capital contribution;
3. Showing the alleged loan as repaid and other illegal practices.

## Section - 68: Ingredients

Key portion of the section read as –

*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....***

## **Ingredients**

The three ingredients of Section 68 are:

### *1. The existence of books of account*

The first ingredient of the section is existence of books of account. In other words, the books of account should be maintained by the concerned assessee. However, books of account of a firm where the assessee is a partner cannot be treated as his personal books of accounts for the purpose of Section 68. *Smt. Shanta Devi v. CIT* [[1988](#)] [171 ITR 532/37 Taxman 104 \(Punj. & Har.\)](#)

### **What may be termed as books of accounts?**

*According to P. Ramanatha Aiyar's Concise Law Dictionary*, unbound sheets of papers in whatever quantity, though filled up with one continuous account are not a book of account. The book of account signifies a collection of sheets of paper bound together with the intention that such binding shall be permanent and the papers used collectively in one volume.

*According to Section 2(12A) of the Income Tax Act, 1961*, books or books of account, includes ledgers, day-books, cash books, account-books and other books, whether kept in the written form or as print-outs of data.

### **Whether Bank Passbook can be regarded as books of account?**

No. *In CIT v. Bhaichand N. Gandhi* [[1983](#)] [141 ITR 67/\[1982\] 11 Taxman 59](#) Hon'ble Bombay High Court held that the passbook supplied by the bank to the assessee cannot be regarded as the books of account of the assessee. In other words, a cash credit of previous year shown in the bank's passbook but not in the cash book maintained by the assessee for that year does not fall under Section 68 and if assessing officer not found suitable explanation can treat it as unexplained money under the said section.

### **Whether rough books can be regarded as books of account?**

Yes. The Hon'ble High Court of Delhi, in *Haji Nazir Hussain v. ITO* [[2004](#)] [91 ITD 42 \(Delhi - Trib.\)](#), held that where assessee failed to give satisfactory explanation for cash credits recorded in his rough books can be assessed as Income of the assessee.

### **Whether a piece of paper found during Search can be regarded as books of account?**

No. Majority of Judges of the Hon'ble Supreme Court in *Shukla (V.C.) JT and L.K Advani on Crl. Revision Petition No. 265 of 1996* held that a piece of paper found in search does not fall within the meaning of "Books of account".

### **2. A credit entry in the said books of account**

The second but most important ingredient is "a Credit Entry." Since the sphere of Section 68 is general and inclusive in nature, the provisions shall apply to all types of credit entries. For Instance, cash credit entry relating to "Gift by ....". In the absence of satisfactory explanation, the tax authorities may construe the said Gift as income from undisclosed sources. Disclosure of gifts in the Income tax returns doesn't validate the gift receipts as lawful income. *State of Karnataka v. Selvi. J. Jaalalitha* [[2017](#)] [392 ITR 97/78 taxmann.com 161 \(SC\)](#).

### **Whether the section covers only credits in cash?**

No. Credits under Section 68 shall include all amounts met for payments found in the assessee's books of account and not merely for cash receipts as loans. In other words, the section itself not confined to cash credits only, say other credits also, for e.g. by way of liabilities also requires satisfactory

explanation, so in its absence, the Assessing officer may add to the income of the assessee. *V.I.S.P. (P.) Ltd. v. CIT* [[2004](#)] [265 ITR 202/136 Taxman 482 \(M.P.\)](#).

### **3. Absence of satisfactory explanation by assessee regarding said cash credit**

The third ingredient says that the assessee offers no proper, reasonable and acceptable as regards the sums found credited in Books of accounts maintained by him in the previous year. For instance, "Gift... By" as stated above, will be taken as absence of satisfactory explanation by the assessee.

#### **Satisfactory explanation by?**

It is clear from the language of the section, it is the assessee, the assessee alone who is to offer the explanation, whether initially or subsequently.

#### **Applicability - Whether retrospective or prospective?**

Section 68 is applicable only from assessment year 1962 - 63 onwards.

#### **Year of Charge**

Since 'Previous year' is now defined to mean only the earlier financial year. In *Bhogilal Virchand v. CIT* [[1981](#)] [127 ITR 591/5 Taxman 65 \(Bom.\)](#) held that effect of the Section is that statutorily, a sum which is found credited in the books of accounts maintained by assessee for any previous year in respect of which either assessee offers no satisfactory explanation or his explanation was not accepted by the assessing officer is required to be charged as income of the assessee of that previous year.

#### **Assessing Officer & His opinion on Cash Credit**

Since "**May**" word has been used in the Section (*fourth line*), it can be easily interpreted as "the Section itself gives discretionary power to apply the provision on a particular sum as income or not. However, even in the absence of satisfactory explanation, it is not necessary to treat all cash credits as income of the assessee. However, the assessing officer cannot act unreasonably and his opinion must be based on relevant factors.

*Hindustan Tea Trading Co. Ltd. v. CIT* [[2003](#)] [263 ITR 289/129 Taxman 601 \(Cal.\)](#).

The Hon'ble Supreme Court, in *CIT v. P. Mohanakala*, [[2007](#)] [161 Taxman 169](#), held that the opinion of the assessing officer is required to be formed with reference to the material available on record.

#### **Burden of proof - On whom? Either on Assessee or the Revenue?**

The issue of cash credit has always been a matter of litigation. The Section enacts a golden rule of evidence which is not in dispute, i.e. the onus is on the assessee to explain any sum found credited in his books of account. However, the section does not absolve the responsibility of assessing officer to prove that cash credit form part of assessee's total income. Further such satisfaction must not be illusory but must have been derived from relevant facts. The amount of cash credits shall not be included in the total income of the assessee if the assessing officer's contention is not justified.

With respect to credits and investments, the Hon'ble Calcutta High Court in *CIT v. Precision Finance (P.) Ltd.* [[1994](#)] [208 ITR 465/\[1995\] 82 Taxman 31](#), laid down that an assessee is expected to establish -

- Identity of creditors
- Capacity of creditors to advance money
- Genuineness of transaction

## Nature and Source

The Hon'ble Bombay High Court, in *Orient Trading Co. Ltd. v. CIT* [1963] 49 ITR 723, had a detailed observation on the nature and source of cash credits under Section 68. The observation, in brief as follows:

*When cash credits appear in the books of account of the assessee, whether in his own name or in the name of third parties, the assessing officer is entrusted to satisfy himself as the true nature and source of such cash credits. In any case, absence of satisfactory explanation by the assessee, the assessing officer is entitled to add back assessee's total income. However, entries stand in third party name, then, issue of question of burden of proof arises. Divergence of opinion expressed over a period of time.*

The Hon'ble Supreme Court in *Kale Khan Mohd. Hanif v. CIT* [1963] 50 ITR 1, held that the onus on the assessee has to be understood with reference to the facts of each case. If the prima facie inference on the fact is that assessee's explanation is satisfactory, the onus shifts to the Revenue.

## Peak Credit Theory

One of the key defence of an assessee, where a single or series of credits entered in the books of account, that a credit following debit entry should be treated as referable to the latter to the extent possible and that not the aggregate but only peak of the credits should be treated as unexplained.

In *Bhaiyalal Shyam Behari v. CIT* [2005] 276 ITR 38 (All.), the assessee claimed the benefit of peak credit theory. The assessee's contention was that the deposits were genuine, so that the benefit of peak credit was an alternative one. Interestingly, the assessee claimed all deposits were genuine and in the same breath asked the benefit of peak credit which is not possible, hence, the Hon'ble Tribunal denied the benefit and the High Court also upheld on the ground that there was no infirmity.

## Appeals - Question of Law and Question of Fact

Cash credit is less a question of law would arise where the decision is based on evidence. The question of the genuineness of a credit or satisfactory explanation by assessee is the question of fact. On whom burden of proof lays also a question of law but whether such onus has been discharged or not is question of fact. *CIT (Central) v. K.S. Dattatreya* [2012] 344 ITR 127/[2011] 197 Taxman 151/9 taxmann.com 106 (Kar.).

*Questions regarding the interpretation of Section 68 are also question of law. CIT v. Smt. Usha Jain* [1990] 182 ITR 437 (Delhi).

In cash credit cases the tribunal is the final fact-finding body and not the High Court. *Balbir sing v. CIT* [2011] 334 ITR 287/196 Taxman 339/[2010] 8 taxmann.com 202 (Punj. & Har.).

## Amendments

### 1. Share application money

In order to prevent generation and circulation of unaccounted money in the case of closely held companies where investments were made by known persons and to place an onus on such companies, two provisions to Section 68 has been inserted vide Finance Act 2012 w.e.f 01.01.2013.

Provisions in brief

In case of any such sum credited as share capital or share premium etc. in the books of closely held company shall be treated as explained satisfactorily, only if the source of funds genuinely explained and proved.

An Exception - Additional onus of satisfactory explanation is not apply, if the shareholder is venture capital fund or venture Capital Company registered with the SEBI.

## **2. Set off Losses against deemed undisclosed Income**

To avoid litigations, the Income Tax Act, 1961 was amended by the Finance Act, 2016. According to amendment to Section 115BBE (2), w.e.f Assessment year 2017-18 onwards, no such set off of loss shall be allowable in respect of income under the Section 68.

## **Judgments In favour of Assessee**

### **1. Geniuses of Credit proved**

The Hon'ble Allahabad High Court in *CIT v. Anurag Agarwal* [\[2015\] 229 Taxman 532](#) ruled in favour of assessee.

Where in respect of credit entries, the assessee established identity of all creditors by providing PANs and addresses beyond reasonable doubts.

### **2. Genuineness of Gift**

The Hon'ble Gujarat High Court in *Smt.Neelamben Gopaldas Agrawal v. ITO* [\[2015\] 57 taxmann.com 176](#), ruled in favour of Assessee.

The said assessee received certain sum as a gift from NRI through banking channels and produced duly certified bank certificates, gift deed etc.

### **3. Genuineness of unsecured Loans**

The Hon'ble Madras High Court in *CIT v. Mark Hospitals (P.) Ltd.* [\[2015\] 232 Taxman 197/58 taxmann.com 226](#) deleted the addition made on account of unsecured loans.

The said assessee had obtained unsecured loans form agriculturists and submitted their details except PANs. The assessing officer made addition under section 68. However, it was found that loans were made through proper banking channels and all creditors had confirmed that they had advanced loans. Since all creditors were agriculturists did not have PAN. On facts addition was deleted.

### **4. Share Application Money - Non-Sufficient of Identifications**

The Hon'ble Supreme Court in *CIT v. Navodaya Castles (P.) Ltd.* [\[2014\] 50 taxmann.com 110/226 Taxman 190 \(Mag.\) \(Delhi\)](#) dismissed a special leave petition against Delhi High Court's impugned order.

The Hon'ble Delhi Court by the impugned order held that certificate of incorporation (COI) and PAN were not sufficient for purpose of identification of Subscriber Company when there was material to show that the subscriber was a paper company and not a genuine investor.

### **5. Surrendered Lesser Amount**

The Hon'ble Rajasthan High Court in *CIT v. Ashok Kumar Jain* [\[2015\] 229 Taxman 65/53 taxmann.com 173/\[2014\] 369 ITR 145](#), ruled in favour.

Whereas in the stated case, the assessee in his revised return surrendered a lesser sum instead of what he had admitted during course of survey. In the absence of assessing officer's to support addition, addition was deleted.

## Judgments In favour of the Revenue

Many judgments are in favour of the revenue. The assessing officers may draw conclusions by using them. Few of them are –

### 1. Onus of proving the source of money

The Apex Court in *Roshan Di Hatti v. CIT* [[1977](#)] [107 ITR 938](#) held that onus of proving the source of a sum of money found to have been received by an assessee is on him. When the nature and source of money or otherwise cannot be satisfactorily explained by the assessee, it is open to the revenue to hold that it is the income of the assessee.

### 2. Third Party Credits

Assessee must prove identities of creditors, capacity of creditors to advance moneys and genuineness of the transactions, then only burden will fall on the revenue.

*Shankar Industries v. CIT* [[1978](#)] [114 ITR 689](#) (The Hon'ble Calcutta High Court)

*CIT v. Biju Patnaik* [[1986](#)] [160 ITR 674/26 Taxman 324](#) (The Hon'ble Supreme Court)

### 3. Genuineness of creditors

In *Mangilal Jain v. ITO* [[2009](#)] [315 ITR 105 \(Mad.\)](#), the assessee failed to prove the genuineness of creditors. Since assessee did not prove the identity of creditor. However, the transaction was by proper banking channel but same was not sufficient. Hence, Hon'ble Madras High Court upheld the additions.

### 4. Filing of Income Tax Return

The Hon'ble High Court of Calcutta, in *CIT v. Korlay Trading Co. Ltd.* [[1998](#)] [232 ITR 820](#), ruled that mere filing of filing of income tax return is not enough to prove genuineness of cash credit.

### 5. Cash Credits through Banking Channels say Cheques

As stated above, the Hon'ble High Court of Calcutta in *Precision Finance (P.) Ltd. (supra)*, held that cash credit can be assessed even if transaction passed through banking channels.

## Concluding Remarks

The Section 68 is really a dynamic one under Indian Income Tax Act. The section is evolving and playing crucial role as far as concerned safeguarding revenue. The aforesaid provisions are making it extremely difficult for assessee or companies to involve in any mala fide practices like tax evasion. It is expected that the above Section and its provision preserve its due place in proposed new Income Tax Law in near future.

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