

Cash Credits & Unexplained Investments - A Walk Down Memory Lane

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Ashish Mehta

Partner, Khaitan & Co.

Cash credits, unexplained investments, unexplained money, etc. have always been highly litigious issues. If one were to look at the way the law and judicial precedents surrounding these issues have evolved and developed over the years, one would surely be reminded of a game of musical chairs. The Income-tax Act, 1961 (**IT Act**) has over the years introduced several provisions to catch-up and at times race ahead in this game. Presently, Sections 68 to 69D of the IT Act (forming part of Chapter VI) are provisions that seek to bring to tax such credits, investments, assets, etc.

While the present sections continue to be marred by debate (as there is still a lot of subjectivity in view of use of the terms like '*explanation offered is not in the opinion of the assessing officer satisfactory*') and controversies over intricate issues surrounding onus, these provisions have in essence even been a part of the erstwhile income-tax legislations enabling revenue authorities bring the so-called unaccounted / unexplained income within the tax net.

Section 68 of the IT Act puts an onus on the taxpayer to satisfactorily explain the nature and source of any credit / assets in his books of accounts or in the possession of the taxpayer. Failure to provide such an explanation may lead to the treatment of such sum / asset as taxable income in the hands of the taxpayer. While each case dealing with additions under these provisions would have some unique features and expositions as these issues are very fact based and circumstances driven, the author has discussed two cases of the Supreme Court of India which have had a huge influence in the way the law as well as later judicial precedents perceived these issues.

Case 1: Durga Prasad More case [\[TS-5156-SC-1971-O\]](#)

Relevant facts and events and the Supreme Court Ruling

1) While the ruling relates to Assessment Year (**AY**) 1958-59 and AY 1959-60, the facts and proceedings of previous years are also relevant and listed below:

a. The assessee in this case had purchased certain premises in the year 1940 for a consideration of INR 1,85,000. It was the assessee's contention that this property was purchased by him in the capacity of a trustee of a trust created by his wife (an oral trust for the benefit of herself and their children).

b. For the first year, income from such property was offered by the assessee in his personal capacity, however for the second year, he did not offer such income pleading that the income did not belong to him in view of a deed of settlement executed by his wife in the year 1941.

c. The assessing officer sought details of source of funds for acquisition of such property. In response, the assessee submitted that the funds used to buy the property were his wife's stridhana (and that INR 2,00,000 was lying with his father-in-law for many years). And that the said INR 2,00,000 was given to him by his wife under the said oral trust.

d. Noting that no credible evidence regarding source (like source of income of wife, money deposited in

bank / advances received from others, etc.) had been placed on record, the assessing officer went on to tax the income from such property in the hands of the assessee.

e. The assessee agitated this in appeals and lost and did not agitate this further before the tribunal.

f. For AYs 1942-43 to 1957-58 the income from the property was assessed in his hands.

2) In the assessment proceedings for AY 1958-59 and 1959-60, the assessee revived his old plea that the income from this property was not assessable in his hands.

3) Assessing officer completed the assessment in line with previous years including such income in his hands. Assessee agitated this before appellate commissioner and then tribunal, but his appeals were summarily rejected in view of the case history namely:

- a. Assessee's wife was not shown to have earned any income to have collected such a huge corpus.
- b. Property was acquired before the purported deed of settlement of trust by the assessee's wife.
- c. Assessee did not explain the source of funds of his wife.
- d. Assessee did not contest the inclusion of income in his hands for 15 (fifteen) years.

4) On further appeal, the Calcutta High Court held in favour of the assessee [\[TS-5328-HC-1967\(CALCUTTA\)-OI\]](#). Although, both judges wrote separate orders. The observations made by the learned judges based on which they gave relief to the assessee are summarized in the table below:

Sr No	Justice A.C. Sen	Justice P.B. Mukherji
1	Apparent statements in the documents must be presumed to be real until contrary is established.	No proof or charge against the assessee that he had concealed his own income.
2	Department did not discharge its onus of showing that income was chargeable.	No evidence of assessee having passed on his income to his wife and concealing his own income
3	Department failed to examine the wife and father-in-law of assessee.	Separate accounts of trust and his own were maintained by the assessee throughout these years.
4	Assessee's own inclusion in earlier years is immaterial as neither res-judicata nor estoppel is applicable to an assessment proceeding.	Assessee did produce sale deed and trust deed when asked by the tax authorities.

5) The Income-tax Department agitated this further and the Supreme Court dealt with each observation of the Calcutta High Court ruling which is summarized below:

On Justice Sen's ruling:

- a. As regards recitals in the deed, the Supreme Court held that a little probing would have proved that what was apparent was not real. It was held that *"The taxing authorities were not required to put on blinkers while looking at the documents produced before them. They were entitled to look into the surrounding circumstances to find out the reality of the recitals made in those documents."*
- b. As regards onus of proof, it was held that the law does not prescribe any quantitative test on whether onus was discharged or not. The arguments of the assessee that his wife had such a huge corpus without any income and it was simply lying in cash with the father-in-law cannot be believed as it does not accord

with human probabilities.

c. Giving relief as wife and father-in-law were not examined was a very superficial way of looking at things.

d. Assessee's act of inclusion of income in the return of income for 15 years could not have been ignored in the name of estoppel / res judicata not being applicable.

On Justice Mukherji's ruling:

a. It was observed by the Supreme Court that there was indeed a charge by the authorities that the assessee was trying to conceal his income in the present case by putting forward a story that the premises were the income of the trust created by his wife.

b. As regards observations regarding concealment of income, the Supreme Court held that the High Court looked at the case from a wrong angle and that in their assessment, the assessee failed to satisfactorily prove that the funds belonged to his wife. The quote from text in this regard is *"Science has not yet invented any instrument to test the reliability of the evidence placed before a court or tribunal. Therefore, the courts and Tribunals have to judge the evidence before them by applying the test of human probabilities. Human minds may differ as to the reliability of a piece of evidence. But in that sphere the decision of the final fact finding authority is made conclusive by law."*

c. Maintaining separate books as well as producing the deeds had much less evidentiary value as compared to the other overwhelming facts which needed to be given credence to.

6) To conclude the apex court held that the Tribunal being the final fact-finding authority had correctly assessed the evidence available and held in favour of the tax department.

This ruling gives an overview of all major arguments available in such matters and throws guidance on how the judges would look at these issues.

Case 2: Sumati Dayal case [\[TS-5013-SC-1995-O\]](#)

This is also a ruling wherein the apex court ultimately held in favour of the tax department after considering all facts and circumstances and reached the conclusion that the propositions of the taxpayer defied human probabilities.

Relevant facts and events and the Supreme Court Ruling

1) This ruling relates to AY 1971-72 and AY 1972-73. The assessee in this case was a dealer in art pieces, antiques, etc. The assessee received INR 3 lakh plus in an year by way of race winnings in Jackpots and Treble events in races at Turf clubs in various cities.

2) Such amount was claimed as not taxable by the assessee, however the assessing officer while passing the assessment order for the year treated the amounts as 'Income from other Sources' and levied tax thereon.

3) Some peculiar facts as listed in the ruling are as under:

a. That the assessee had sworn an affidavit wherein it was stated that she had begun going for races only in the end of the year 1969 and had no previous experience.

b. The assessee claimed to have won a sum in excess of INR 3 lakh in one year on thirteen occasion out of which ten were winnings from jackpots and three were treble events. In the other year, an aggregate of INR 1 lakh approximately was earned on two occasions being jackpot winnings.

c. That the assessee won a jackpot on the first day she went to the races.

d. The assessee stated that she worked out the combination on the basis of what her husband advised

her and she also used to add a few horses of her own although she admitted that she did not know anything about the performance of these horses before the December of 1969.

e. The books of accounts of the assessee did not reflect drawings commensurate with the amounts that would be required to purchase the tickets for these races and related events.

f. While the capital account of the assessee were credited with the sums of winnings, there were no debits or expenses for purchase of tickets or losses incurred on races.

g. Winning from races became taxable from 1972 (vide an amendment treating the same as income), after such date, the assessee gave up the activity, which was found to be very strange given her exceptional luck and track record.

h. When the matter was before the settlement commission, the assessee offered to agree to a reasonable addition towards inadequate drawings if the settlement commission were to come to hold in her favour on merits of the case.

4) Based on the above findings the assessing authorities as well as the Settlement Commission was of the view that given the meagre knowledge the assessee had as well as the complexities involved for winning jackpots. It was observed that *"A Jackpot is a stake of five events in a single day and one can believe a regular and experienced punter clearing a Jackpot occasionally but the claim of the appellant to have won a number of Jackpots in three or four seasons not merely at one place but at three different centres, namely, Madras, Bangalore and Hyderabad appears, prima facie, to be wild and contrary to the statistical theories and experience of the frequencies and probabilities."*

5) While the settlement commission held by majority that the facts stated by the assessee were devoid of human probabilities, the chairman of the Settlement Commission in his dissenting opinion mentioned that the payments were received by crossed cheques for payments of amounts toward winning of jackpots and also that in such a game of chance, expertise was not necessary. This dissenting opinion of the chairman was termed as a superficial approach by the Supreme Court and it was held that one needs to consider the matter in the light of human probabilities.

6) The Supreme Court held that having seen the entire factual matrix, an inference could be reasonably drawn that the winning tickets were purchased by the assessee after the events. The Supreme Court observed that such activities were prevalent and referred to the District Taxes Enquiry Committee and the recommendations made by the said Committee which led to the amendment of the Act by the Finance Act, 1972 whereby the exemption from tax that was available in respect of winnings from lotteries, crossword puzzles, races, etc., was withdrawn.

7) As regard onus of proof on the department that this was undisclosed income of the assessee and routed as lottery / jackpot winnings, the Supreme Court has observed that direct evidence about such acts would not be available as such events take place in secret.

Thus, it will be observed that even in this case the Supreme Court has given credence to the factual position as well as events surrounding these facts rather than go on a superficial approach and rely merely on the tangible evidences placed before them (like crossed cheques, copies of winning tickets, etc. produced by the assessee). The Supreme Court has unequivocally held that in such cases it would be impossible for the tax department to produce clinching evidence in support of their claims of tax evasion. Thus, such a superficial approach should not be adopted by the authorities and courts.

Conclusion

While it has been consistently held that in cases where a receipt is sought to be taxed as income, the burden lies on the department to prove that it is within the taxing provisions, it is equally true that if a receipt is in the nature of income, the burden of proving that it is not taxable because it falls within an exemption provided by the IT Act lies heavily upon the taxpayers. The likes of Section 68, 69, 69A, 69B, 69C however would require that where any sum is found credited in the books of a taxpayer (or assets are found in possession of the taxpayer) the same may be charged to income-tax as income if the explanation offered by the taxpayer about the nature and source thereof is, in the opinion of the

assessing officer, not satisfactory. In such case there is, prima facie, evidence against the taxpayer, viz., the receipt of money, and if he fails to rebut, the said evidence being unrebutted, can be used against him by holding that it was a receipt in nature of income.

The Supreme Court in the above discussed cases as well as in a number of cases upheld substance over form and held that the perfect and clinching evidence regarding tax evasion may not be available in every case and that the matters should then be adjudicated on the basis of surrounding circumstances and 'Theory of Human Probabilities'. These cases and theories have been referred to in a number of later rulings dealing with bogus capital gains in penny stocks, investment in shares at unjustifiably high premiums, gift receipts from unexplained sources, etc. and in these cases, the courts have time and again given credence to substance over form.