

AO was justified in rejecting books of account if assessee failed to produce books during scrutiny assessment

Summary – The Rajkot ITAT in a recent case of Smt. Jayaben K. Ghelani, (the Assessee) held that where assessee failed to produce relevant books of account in scrutiny assessment, Assessing Officer was justified in rejecting book results and making addition on estimation basis under section 145(3)

Facts

- The assessee was engaged in trading of iron scrap. She filed her return declaring certain income. The case of the assessee was selected for scrutiny assessment and notice under section 143(2) was duly served. Thereafter, the Assessing Officer issued various notices, but the assessee did not submit requisite details.
- The Assessing Officer thus estimated the income as per section 145(3). The Assessing Officer noted that the assessee had declared GP at the rate of 3.81 per cent on turnover. He further observed that in the immediately preceding year, profit disclosed by the assessee was 4.21 per cent. Since the assessee failed to produce books of account and other details, the Assessing Officer estimated GP at 20 per cent of turnover, and, accordingly, made addition to assessee's income.
- The Commissioner (Appeals) took a view that when books of account were not produced before the Assessing Officer, he could not reject the same and proceed to make estimated addition. Accordingly, the addition made by Assessing Officer was deleted.
- On revenue's appeal:

Held

- A bare reading of section 145 would reveal that it provides the mechanism how to compute the income of the assessee. According to sub-section (1), the income chargeable under the head 'profit and gains of business or profession' or 'income from other source' shall be computed in accordance with the method of accountancy employed by an assessee regularly, subject to sub-section (2) of section 145. Sub-section (2) provides that the Central Government may notify in the official gazette from time to time, the Accounting Standard required to be followed by any class of assessee in respect of any class of income. Thus, it indicates that income has to be computed in accordance with the method of accountancy followed by an assessee *i.e.* cash or mercantile, such method has to be followed keeping in view the Accounting Standard notified by the Central Government from time to time.
- Sub-clause (3) provides a situation, that is, if the Assessing Officer is unable to deduce the true income, on the basis of method of accountancy followed by an assessee he can reject the book result and the assessee's income according to his estimation or according to his best judgment. The

Assessing Officer in that case is required to point out the defects in the accounts of assessee and required to seek explanation of the assessee *qua* those defects. If the assessee has failed to explain the defects and on the basis of the book result, income cannot be determined, the Assessing Officer would compute the income according to his estimation keeping in view the guiding factor for estimating such income.

- For exercising the best judgment, section 144 provides the guidance to the Assessing Officer . It is pertinent to note that that section 144 would suggest that in order to estimate income, the Assessing Officer has to exercise his discretion which should be in consonance with best of his judgment. In various authoritative pronouncements, it has been propounded that in making a best judgment assessment, the Assessing Officer must not act dishonestly or vindictively or capriciously. He must make, what he honestly believes to be a fair estimate of the proper figure of assessment and for this purpose he must be able to take into consideration, local knowledge, reputation of the assessee about his business, the previous history of the assessee or the similarly situated assessee.
- It is also pertinent to mention that judgment is a faculty to decide matter with wisdom, truly and legally. Judgment does not depend upon the arbitrary caprice of an adjudicator, but on settled and invariably principles of justice. Thus, in a best judgment, even if, there is an element of guesswork, it should not be a wild one, but shall have reasonable nexus to the available material and circumstances of each assessee.
- In the light of the above, if one examines facts of the instant case, then it would reveal that the Commissioner (Appeals) has erred in observing that section 145(3) could not be applied in this case, because, Assessing Officer could not examine records as those accounts were not produced before him. Section 145(3) contemplates that the Assessing Officer can resort to estimate the income, if he is unable to deduce true result from the accounts or other details. Strictly, books were not produced before the Assessing Officer, it was not rejection of books as such, but impliedly it was estimation of income as per section 145(3).
- The Commissioner (Appeals) has not considered any of these aspects, *viz.* why there is a decline in GP, why assessee does not want to scrutinise its books of account from the Assessing Officer. Therefore, considering all these aspects, the order of the Commissioner (Appeals) is not sustainable. Total addition cannot be deleted. As observed above, income even after rejection of books can be estimated on some guesswork. It is to be estimated keeping in view surrounding facts and circumstances. In the present case, the assessee herself had shown GP at 4.21 per cent in the immediately preceding year. Therefore, the Assessing Officer ought to have adopted GP nearby this figure and not at 20 per cent. The assessee in her submission before the Commissioner (Appeals) has expressed the rate of at 4.25 per cent.
- Thus, taking into consideration submissions filed by the assessee before the Commissioner (Appeals) and other material, it is appropriate that ends of justice would be met, if the gross profit was calculated at the rate of 5.5 per cent of the total turnover. With the above observation, impugned

order of the Commissioner (Appeals) is set aside and the Assessing Officer is directed to recalculate the addition by applying GP at 5.5 per cent of the total turnover.

- In the result, the appeal of the revenue is partly allowed for statistical purpose.