

**IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH "D", MUMBAI**

**BEFORE SHRI ABY T. VARKEY, HON'BLE JUDICIAL MEMBER AND
SHRI S. RIFAUR RAHMAN, HON'BLE ACCOUNTANT MEMBER**

**ITA.NOs. 2654 & 3251/MUM/2019
(A.Y: 2013-14 & 2014-15)**

ACIT- Central Circle-15(1)(2) Room No. 483A, 4 th Floor Aayakar Bhavan, M.K. Road Mumbai – 400020	v.	M/s. Desh Consultancy Services Pvt. Ltd., 101-105, B-Shiv Chambers, Sector -11 CBD Belapur, Navi Mumbai-400614 PAN: AACCD0044L
(Appellant)		(Respondent)

Assessee Represented by	:	Shri Shivram & Shri S.L. Jain
Department Represented by	:	Smt Mahita Nair
Date of Hearing	:	16.01.2023
Date of Pronouncement	:	03.03.2023

ORDER

PER S. RIFAUR RAHMAN (AM)

1. These appeals are filed by the Revenue against different orders of the Learned Commissioner of Income Tax (Appeals)-24, Mumbai [hereinafter in short "Ld.CIT(A)"] dated 31.01.2019 and 01.02.2019 for the A.Y.2013-14 and A.Y. 2014-15 respectively.

2. Since the issues raised in both these appeals are identical, therefore, for the sake of convenience, these appeals are clubbed, heard and disposed off by this consolidated order. We are taking Appeal in ITA.No. 2654/MUM/2019 for Assessment Year 2013-14 as a lead appeal.

3. Brief facts of the case are, assessee filed its return of income on 28.09.2013 declaring loss of ₹.2,23,46,102/-. Subsequently, the case was selected for scrutiny and notice u/s.143 (2) and 142(1) of Income-tax Act, 1961 (in short "Act") were issued and served on the assessee along with the questionnaire. In response authorised representative of the assessee attended and submitted the relevant information as called for.

4. The Assessee is in the business of Subscriber to chit fund and the Assessing Officer himself observed that there is no material change in the business of the Assessee as compared to the earlier assessment year. During the course of assessment, the Assessee was asked to submit the details of the nature of business and accordingly assessee submitted vide letter dated 12.01.2016 a note on the bidding system followed and how dividends are being generated. Further, assessee submitted that assessee has placed a security deposit of ₹.6,59,58,457/- with

M/s.Shriram Chits (Maharashtra) Limited [SCML] for the future installments of subscription payable. Further, assessee submitted that the chit prize money receivable shown in the Balance Sheet which is said to be the prize money receivable from SCML as on 31.03.2013. Assessing Officer observed from the submissions of the assessee that assessee invested in the chits of SCML and incurring huge discounts to the tune of ₹.9,08,58,239/- against which the dividend income received on chits are only ₹.5,60,85.485/- in addition to the interest and finance charges on the security deposit of ₹.89,69,270/-. The Assessing Officer rejected the submissions made by the assessee with the observation that business prudence, especially due to the fact that the majority of the shareholding of the assessee is with SCML and no owner will keep on making investments to earn losses and accordingly, the assessee was issued with a notice u/s. 142(1) of the Act calling for the party wise details along with address and PAN in respect of chit account, chit prize money receivable, other receivables, unmatured discount on chits, discount on prizing chits etc.

5. In response to the above notice, assessee vide letter dated 27.01.2016 submitted that the amount receivable as well as payable in

respect of all these transaction appearing in the Balance Sheet are from/to SCML only. The Assessing Officer observed that inspite of repeated opportunities, Assessee has not furnished any details in respect of the various chits in which they have subscribed and what are the utilization of the funds received from SCML. Further, he observed that assessee filed a note on the chit prize money receivable wherein the additions during the year have been mentioned as various branches and different amounts. No evidence in this regard has been filed by the assessee. In view of the above, the Assessing Officer issued another show cause notice as to why the discount on chit amounting to ₹.9,08,58,239/ should not be disallowed. In response, assessee filed a letter containing the note on the procedure being followed in respect of subscription of chits and further submitted that the method of accounting and method of calculation of discount was applied pro rata for the financial year and prayed that the same may be allowed as revenue expenses.

6. After considering the submissions of the assessee, Assessing Officer rejected the same with the observation that assessee has not brought any evidence on record to show that they have invested in a number of chits and has incurred such a huge discount as mentioned above. In this

connection, he relied on the decision of Hon'ble Kerala High Court decision in the case of Ram Bahadur Thakur Ltd., [261 ITR 390]. Since assessee has not furnished any evidence with regard to the investments in various chits and that the discount debited on prizing chits debited to the Profit and Loss Account in respect of amount payable pertaining to the Financial Year 2012-13 and accordingly disallowed the discount claimed by the assessee and added back to the income of the assessee.

7. Further, Assessing Officer observed that assessee submitted vide its letter dated 05.02.2016 the details of month wise bidding of chits. On perusal of the same, he observed that assessee receives the chit value invested by the investors as its income. From the said income the assessee incurred certain expenditure viz., Bid Amount, Prize Money on the chits, Subscription arrear, Current Sub & VC charges and Service Tax. He observed that after deducting the above amounts from the receipts and the balance amount, which is actually is the net profit of the assessee company. For the year under consideration the left over/surplus of income over expenses available with the assessee company is at ₹.5,97,49,414/. He observed that this amount is purely the profit of the assessee as it is arrived after deducting the entire expenses pertaining to

the chit business. However, assessee has shown a total receipt of ₹:5,60,85,485/-. Therefore, the difference amount of ₹.36,63,929/- is added to the total income of the assessee.

8. Aggrieved assessee preferred an appeal before the Ld.CIT(A) and filed detailed submissions along with the details of investment in various chits and discount debited on prized chits before the Ld.CIT(A), for the sake of clarity it is reproduced below: -

"It is an appeal filed against assessment order as passed by Ld. Assessing Officer u/s.143(3) dtd. 14.3.16. Appellant filed its return of income declaring a loss of Rs.22346102/- Ld. AO has completed the assessment at an income of Rs. 7,21,76,070/-. While completing the assessment Ld. AO disallowed discount borne by the appellant in bidding the chits of Rs.9,08,58,239/- and also made an addition to the income of the appellant of Rs. 36,63,929/-. This appeal is filed against these additions made by Ld. AO.

1. Ground no. 1 to ground no.5 deals with disallowance of discount of Rs.9,08,58,239/- by Ld. AO. Ld. AO has stated that business of the appellant is of subscriber to chit funds and there is no material change in the business of appellant. It is further stated that during the course of assessment proceedings, appellant submitted a note on the bidding system and how dividend is generated. The appellant further submitted that chit price money receivable as reflected in balance sheet is receivable from M/s. Shriram Chit (Maharashtra) Ltd and it has subscribed to the chits issued by the said company. In para-4 Ld. AO concluded that appellant had incurred huge discount of Rs.9,08,58,239/- against which it has received dividend of Rs. 5,60,85,485/- and interest on security deposit of Rs.89,69,270/- Hence, submission of the appellant cannot be accepted as business prudence, especially due to the fact that majority of the shareholders of the appellant is M/s. Shriram Chit (Maharashtra) Ltd. It is further stated that appellant company was issued a notice u/s 142(1) calling upon the appellant to file (partywise details alongwith address and PAN in respect of chit account (ii) chit price money receivable (iii) other receivables (iv)

unmatured discount of chits (v) discount on prizing chit Appellant under its letter dtd 27.1.16 wherein it was explained that all these transactions are carried out with M/s. Shriram Chit (Maharashtra) Ltd as appearing in balance sheet. Ld. AO thereafter concluded that inspite of repeated opportunity appellant has failed to furnish details in respect of various chits in which they have subscribed. Appellant filed a Note on chit price money receivable, wherein the addition during the year has been mentioned. No evidence in regards has been filed by the appellant. Hence appellant was given a show cause notice why discount on chit amount Rs.9,08,58,239/- should not be disallowed. Appellant filed a letter containing a Note on the procedure being followed in respect of subscription of chits and relied assessment order for AY 03-04 for its method of accounting and method of calculation of discount Thereafter Ld. AO relied upon the decision of Rambahadur Thakur Ltd- 261 ITR 390 (Kerala) and concluded in para-4.4 that appellant has not furnished (0) evidence with regards to investment in various chits (ii) discount debited on pricing chit as debited to P&L A/c for the FY. and made the disallowance.

1.1 Ld. AO has also made addition of Rs. 36,63,929/- to income. Ld. AO stated that appellant company vide its letter dtd. 5.2.16 submitted details bidding on chits which gives the details of bid amount etc. The left-over surplus after reducing the expenses in chit amount is Rs. 5,97,49,414/- which as per Ld. AO is profit of the appellant against which appellant has shown receipt of dividend Rs.5,60,85,485/- and hence the difference between two Rs.36,63,929/- is being added to the income of the appellant.

2. We have honour to submit that discount as debited in P&L A/c of Rs.9,08,58,239/- is being disallowed by Ld. AO by relying upon the decision of Rambahadur Thakur Ltd- 261 ITR 390 (Kerala). The court held that in view of the provisions of Sec 40A(2) It is open to taxing authority to go into reasonableness of expenses and to see the commercial necessity of spending. Ld, AO in para-4 stated that as majority of share holding of appellant is held by Shriram Chit (Maharashtra) Ltd, the discount is disallowable. The details of shareholding of appellant is provided in audited accounts as filed before Ld. AO, which shows that no share is being held by Shriram Chit (Maharashtra) Ltd (pg. 12). On page-44 the details of shareholding of Shriram Chit (Maharashtra) Ltd is given and on page-45 shareholders of the appellant. A reference to the same will show that appellant is not associated within the meaning of Sec. 40A(2) of I.T. Act with Shriram Chit (Maharashtra) Ltd and hence, the said observation of Ld.AO are inapplicable and no disallowance should have been made by reference to the said decision of Kerala high

court or on the basis that shareholding of the appellant is held by Shriram Chit (Maharashtra) Ltd.

2.1 The other reasons given by Ld AO in para-44 is that appellant has not furnished the evidence with regards to (1) investment in various chits (1) discount debited on price chits as debited to P&L A/c. It is most respectfully submitted that a notice u/s. 142(1) in the form of Questionnaire was issued dtd. 21.7.15. It was a general questionnaire (pg. 20-23). Appellant filed its reply dtd. 7.8.15 giving a Note on business activities in the form of an annexed Note, which states that business of the appellant is subscribing to the chit funds and has described the procedure followed in subscribing the chits; how the chits are auctioned and acquired in bidding and how the discount are borne (pg.26-27). It has also stated that there is no associate concern (24-25). It is confirmed that there is no payment made to persons covered u/s.40A(2)(b) (pg. 25-27). Under submission dtd. 12.1.16 appellant submitted details of chit subscription payable Rs.3,49,79,162/- A note on unmatured discount on chits (pg. 28-29). In the note on unmatured discount of chit, appellant explained the methodology to claim the discount in various AYS (pg.30).

Ld. AO thereafter issued a notice u/s 142(1) dtd. 23.1.16 requiring the appellant to furnish the details of (1) liability on account of chit subscription Rs. 11.35 crs. (ii) unmatured discount reflected of Rs.9.56 crs. (ii) partywise details of revenue from operation (iv) partywise break-up of discount on chits (pg.32-33).

Appellant filed its submission dtd. 5.2.16 under which it submitted the details of (1) long term liabilities that the chits account Rs.11.35 crs. (pg.38) (i) breakup of unmatured discount on chits (pg.39) (i) partywise details of revenue from operations (pg. 40) (iv) partywise breakup up of discount on chits (40). In the said submission it also referred to the procedure followed for chit discount and how the discount as debited to P&L A/c. of Rs.9.08 crs. is computed on proportionate basis (pg.34-37).

Appellant under letter dtd. 27.1.16 (9.173) submitted (i) chit report (A) (dividend report (B) (iii) unmatured discount on chits (C) Appellant filed complete details of chit liabilities Rs.26.28 crs. In the audited accounts, liability of Rs.11.35 crs. is reflected under the head 'long term liabilities' and Rs: 14.93 crs. is reflected under current liabilities. Thus, the appellant has filed complete details of chits subscribed. Under report of dividend (B), it gives complete details of dividend received on various chits of Rs.5.60 crs. and under report for unmatured discount in Schedule-C it gives complete details of

Rs.9.56 cr. unmatured discount, giving chit-wise details. Thus, it is most respectfully submitted that appellant has filed complete details of investments in chits, liability payable thereon and discount debited on prizing chits. Appellant was not called upon to file any further details during the course of assessment proceedings. Appellant has submitted all the details as called for.

Appellant submitted details of various chits which has been obtained by the appellant by bidding during the year and discount borne by appellant on the same. The details provided the name of branch, chit numbers, face value, number of months for which the chit is issued, discount borne by the appellant, how many months are left in current year, based on which discount is claimed during the year and in subsequent years. Out of the total discount borne by the appellant on various chits obtained in auction to be Rs. 10,8 crs. in current year, out of which Rs.5.36 crs, discount is claimed in current year and balance discount is claimed in subsequent AYS e. AY 14-15, 15-16 & 16-17 (pg. 46-89). From the details of discount claimed it will be observed that in current year, out of Rs. 10.80 crs. appellant has claimed Rs.5.36 crs. and balance amount relates to earlier years.

2.2 Procedure of discount on bidding of chits can be explained by way of an example:

A foreman in present case Shriram Chit (Maharashtra) Ltd conducting the chit enters into agreement with a specific number of subscribers, every subscriber shall subscribe periodically, a definite sum of money, over the specific period. An auction is conducted in each month and any one of the subscriber can bid to receive the collection of that month by offering a discount. Such discount offered is known as 'discount on prizing chit' and amount received is called chit prize! An example can be given to explain as under-

'A typical case would be 40 subscribers participation in a chit group for 40 month, each subscriber contribution a monthly subscription of Rs. 250/- The total chit amount that will be collected each month will be Rs.10,000/- Normally every month an auction will be conducted and every subscriber is entitled to bid at the auction, subject to commission in favour of the foreman who runs the chit transaction. If in chit group starts, say, on 01.04.2012, the chit group will end by 31.07.2012, if in the 9 auction, a subscriber 'X' the absence of any higher offer of discount of Rs.2,000/- and a subscriber 'Y' will be successful bidder. If 'Y' is declared as a successful bidder, the following situation emerges.

a) "Y" will be the successful bidder.

- b) "Y" is entitled to receive Rs 7,600/- being the difference between the chit amount of Rs. 10000/- (-) discount Rs. 2400/- Rs. 7600/- called the "Prize Amount"
- c) Out of the discount of Rs.2400/- the foreman, will be entitled to Rs.500/- as his commission being 5% of the chit amount. d. The balance of Rs. 1,900/- (Rs. 2,400-Rs.500) will be distributed as
- d) dividend between the 40 subscribers at Rs. 47.50/- each.
- e) The successful bidder 'Y' has got the only obligation to continue to pay the chit subscription of Rs.250/- per month for the remaining 31 months with a right to get dividend for each of the remaining months could be adjusted against the monthly subscription. The successful bidder is called the "Prized Subscriber and his obligation regarding the remaining months is no different from that of non-prized subscriber. His only obligation financially is to pay his further subscription regularly vide section 25 of the Chit Funds Act, 1974

It is submitted that discount is given in lieu of getting the money in advance and hence a is opportunity cost. Appellant also referred that issue was first time considered in assessment proceeding for AY 03-04, when the assessment was completed u/s 143(3). Ld. AO while making the assessment held that discount will be allowable on prorata basis for the period falling during each assessment year the discount relating to all subsequent years will be allowable in such subsequent year i.e. on % percentage completion method. The procedure is explained in said order (pg. 41-43). Appellant thereafter followed the said method, instead of claiming whole of the discount in the year incurred on completion method Appellant has claimed proportionate discount. It is most respectfully submitted that appellant filled all the details during the course of assessment proceeding. It was clarified that all its chit transactions are with M/s Shriram chits (Maharashtra) Ltd. PAN AAEGS75929 No further details were called for, Thus Ld. AO eared in making disallowance for want of details.

2.3 Thus it is most respectfully submitted that discount bome by the appellant on chits is allowable discount. Appellant has followed the method for claiming discount as approved by Ld. AO in AY 03-

04. Thereafter continuously appellant has been following the same method and has been accepted till AY 10-11. While making the assessment for AY 11-12, the discount claimed by the appellant was rejected Hon. ITAT while approving the method of accounting, followed by the appellant has set aside the issue to your honour's file for verification of the details, as Ld. AO disallowed the claim for want of details. A copy of Hon. ITAT order is enclosed.

2.4 In view of this, it is most respectfully submitted that appellant has submitted all details during the course of assessment proceedings as called for, books of the appellant are audited, all the transactions of subscription of chits, its bidding and discounting is carried by the appellant through SCML, a company assessed to tax under PAN: AAEC7592Q Complete details of discount of Rs.9.56 crs was submitted under letter dtd: 27.1.16; books of accounts of appellant are audited; appellant has submitted copies of certain chit agreements by way of sample (pg. 91-172); chit agreements are similar to as entered in earlier years. Hence, it is most respectfully submitted that discount claimed during the year is fully recorded in the books of accounts and all the requisite details has been submitted. Before your honour appellant has submitted a chit-wise details of all chits discounted during the year and how the discount is claimed in current year and subsequent years (pg.46-89) to clarify the issue further. In view of this, it is most respectfully submitted that discount is allowable to the appellant.

3. Under ground no.6 appellant has challenged the addition made of Rs.36,63,929 Ld. AO stated in para-5 that appellant has received bid amount after all necessary deduction of Rs 5,97,49,514, which is of the nature of income. Appellant declared dividend receipt of Rs 5,60,85,485/4 Difference between two is assessed as income Rs.36,63 929/

3.1 It is submitted that after bidding a chit, under the provisions of Sec. 31 of Chit Fund Act, appellant is under obligation to pay subscription for remaining period of the chit. Under the provisions of Sec. 31 of Chit Fund Act, the prized subscriber is required also to get deducted future subscription for chit out of the prized amount or to furnish sufficient security for payment of all future subscription. Sec 31 runs as "Every prized subscriber shall, if he has not offered to deduct the amount of all future subscriptions from the prize amount due to him, furnish, and a foreman shall take sufficient security for the due payment of all future subscription and, if the foreman is a prized subscriber, he shall give security for the due payment of all the future subscriptions to the satisfaction of the Registrar

Thus, the amount received by the appellant in auction by way of chit is not of the nature of income; but it is the liability as appellant is to pay subscription for further months. Hence, Ld. AO erred in holding the amount received of chit as appellant's income. Hence, it is most respectfully submitted that addition made to the income of Rs.36,63,929/- is uncalled for. A similar issue is considered by Hon. CIT(A) in appellate order for AY 12-13 in para-2.4.4 onward. A copy of order is enclosed herewith."

The appellant further submitted written submission as under:

"1. Ld. Assessing Officer disallowed discount with observation in para 4.4 "As the Assessee Company has not furnished any evidence with regard to the investments in various chits and that the discount debited on prizing chits debited to the Profit & Loss A/c. is in respect of the amount payable pertaining to the financial year 2012-13 (the discount on prizing chits are claimed on pro rata basis only). I have no other option but to disallow the discount on prizing chits claim made in the return of income. Accordingly, the discount prizing chits amounting to Rs.9,08,58,239 is disallowed and added back to the total income of the Assessee Company."

1.1 It is submitted that appellant submitted various details during the course of assessment proceedings as to i. Investments in various chits ii. discount debited on price chits

(i) Under letter dated 27/01/2016 chit wise details was submitted of chits in operation of Rs.67,81,20,200/-, subscription paid Rs. 41,52,95,370- and subscription payable as on 31/03/2013 of Rs.26,28,24,830/- liability of Rs 26,28,24,830/- includes Rs 11,35,72,350/- being Long Term liability payable and Rs.14,92,52,500/- as current liability for chit subscription payable. These details includes chits subscribed during the current year (pg. 173 A)

(ii) complete list of dividend received giving chit number and amount of dividend received during the year of Rs.5,60,85,485/- (pg.173 B) and (iii)complete details of unabsorbed discount on chits giving chit numbers and amount of unabsorbed discount amount to Rs.9,56,80,648/- (pg. 173C). Thus complete details of chit subscribed as well as discount were submitted.

(iii) The appellant submitted also details as called for by Ld. Assessing Officer from time to time. A note on chit business was submitted under letter dated 07/08/2015

giving an illustration how chits are subscribed, discounted and the nature of discount (pg.26 27), a note on unmatured discount under letter dated 12/01/2016 (pg.30), chit discount was also explained under letter dated 05/02/2016 (pg.36-37) and party wise details were submitted specifying that all the chit transactions were carried out through Shriram Chits Maharashtra Ltd., PAN:AAECS7592 Q

Before your Honour chit wise details of all the chits discounted during the year are submitted giving details of chits subscribed and discounted during the year discount bore of Rs. 10,80,03,880/- out of which Rs. 5,36,72,780/- is claimed in the current year and balance is claimed in the assessment year 2014-15 onwards on period basis. Details of chits subscribed and discounted are already contained in Annexure A, B, C as submitted by the appellant. Ld. Assessing Officer just followed the earlier year assessment order and made the disallowance on the plea of non- filing of details while all the details were submitted.

2. The Ld. Assessing Officer has relied upon the decision of Ram Bahadur Thakur Ltd., 261 ITR 390 Kerala for the proposition that payment being made to an associate concern covered under Sec. 40A(2) and payment being disproportion to income earned the same is not allowable. Under submissions dated 07/08/2015, the appellant submitted that it has no associate concern (pg.24) and payment of discount is not to Shriram Chits (Maharashtra) Ltd.

2.1 The chit transaction are governed under The Chit Fund ACT 1982. Certain provisions of Act require consideration. which shows that discount borne by appellant is not paid to Shriram Chits Maharashtra Ltd. The following terms are defined u/s 2 of the said Act:

(c) "chit agreement" means the document containing the articles of agreement between the foreman and the subscribers relating to the chit;

(g) "discount" means the sum of money or the quantity of grain which a prized subscriber is, under the terms of the chit agreement, required to forego and which is set apart under the said agreement to meet the expenses of running the chit or for distribution among the subscribers or for both;

(h) "dividend" means the share of the subscriber in the amount of discount available under the chit agreement for rateable distribution among the subscribers at each instalment of the chit;

(j) "foreman" means the person who under the chit agreement is responsible for the conduct of the chit and includes any person discharging the functions of the foreman under section 39,

(m) "prize amount means the difference between the chit amount and the discount, and in the case of a fraction of a ticket means the difference between the chit amount and the discount proportionate to the fraction of the ticket, and when the prize amount is payable otherwise than in cash, the value of the prizes amount shall be the value at the time when it becomes payable;

(n) *prized subscriber* means a subscriber who has either received or is entitled to receive the prize amount;

In this case Shriram Chit is Forman, it has to enter in agreements with each subscriber for each chit, under sec 4 state government permission is required to commence a chit, under sec 6 every chit agreement shall be in duplicate and shall be signed by each of the subscribers and the foreman and attested by at least two witnesses the probable date of commencement and the duration of the chit, it will contain prescribed particulars; duration of a chit shall not extend beyond a period of five years from the date of its commencement, the amount of discount referred to in clause (f) of sub-section (1) shall not exceed '[thirty per cent.] of the chit amount, where the prized subscriber at any instalment of the chit is required to be determined by auction and more than one person offer the maximum discount, the prized subscriber shall be determined by lot. As per sec 7 every chit agreement shall be filed in duplicate by the foreman with the Registrar who will register the same. Under sec21 the foreman shall be entitled to such amount not exceeding five per cent. of the chit amount as may be fixed in the chit agreement, by way of commission, remuneration or for meeting the expenses of running the chit, to receive and realise all subscriptions from the subscribers and to distribute the prize amounts to the prized subscribers, to demand sufficient security from any prized subscriber for the due payment of future subscriptions payable by him. Sec31 provides that every prized subscriber shall, if he has not offered to deduct the amount of all future subscriptions from the prize amount due to him, furnish, and a foreman shall take, sufficient security for the due payment of all future subscriptions and, if the foreman is a prized subscriber, he shall give security for the due payment of all the future subscriptions to the satisfaction of the Registrar. Every prized subscriber shall pay his subscriptions regularly on the dates and times and at the place mentioned in the chit agreement and, on his failure to do so, he shall be liable to make a consolidated payment of all the future subscriptions forthwith.

2.2 The operation of Chits is considered in certain decided cases as in the case of *Bilahari Investment Pvt. Ltd.*, 299 ITR Supreme Court describe the nature of chit business in para "5. Chit funds are basically saving schemes in which certain number of subscribers join together and each contributes a certain fixed sum each month, the total number of months being equal to the total number of subscribers. The subscriptions are paid to the manager of the fund by a certain prescribed date each month and the total subscriptions to the fund are auctioned each month amongst the subscribers. At each auction, the lowest bidder is paid the amount of his bid and the balance received from out of the total subscriptions received is distributed equally amongst other subscribers, as premium. The manager is paid a certain percentage of the collections each month on account of expenses and charges for conducting the auction. In the auction, a maximum amount, which the highest bidder agrees to forego, is the amount, which is distributed to the other members, subject to deduction of the manager's commission. The Court held that claim of the discount is allowable as business expense and dividend received on chits is taxable as business income."

2.3 The High Court in the case of *Sahib Chits (Delhi) Pvt. Ltd.* 328 ITR 342(del), in para 5 considered the nature of discount suffered by the chit subscriber that "The person who gives the highest bid is entitled to take a particular chit. The amount of bid offered by him is distributed between the members/subscribers. These chits are governed by the law known as the Madras Chit Funds Act, 1961, which is extended to the Union Territory of Delhi. As per the provisions of this Act, there is a restriction to make a bid upto 35 per cent of the maximum value of the chit. If more than one person offered 35 per cent, then between them chit is allocated to a person by a draw of lot. The bid amount offered by the successful bidder is then distributed equally among all the members. It is this amount which is paid to the members that is treated as 'interest' by the AO. On this premise, the AO proceeded and opined that before disbursing this amount of interest' to the members/subscribers, the assessee was required to deduct tax at source under s. 194A of the Act and held that for not doing so it committed default and, therefore, was liable for interest and penalty under s. 201/201(1A) of the Act." In para 9 the court held following the pre of "Madras Chit Funds Act, 1961, as extended to the Union Territory of Delhi (Madras Act 24 of 1961) "the share of a subscriber in the discount available under the chit agreement for rateable distribution among the subscribers at each instalment of the chit."

2.4 In the case of *SHRIRAM CHITS (P) LTD.* 79 TTJ 0598 Hyderabad, the bench described the operation of chits in para "5 The

modus operandi of the chit business can be explained by way of this example, given below:-

If the chit group promoted by the company is Rs. 50,000 prize money for 50 months then 50 subscribers join this chit group and each one of them is supposed to contribute Rs. 1,000 per month. Every month there will be an auction of this chit and the successful bidder will get the prize money less discount offered by him. Thus, if subscriber-A were to bid Rs. 50,000 for Rs. 40,000, he will be offering a discount of Rs. 10,000, He will get the prize amount of Rs. 40,000 only. The foreman will be getting 5 per cent of Rs. 50,000 as commission i.e.. Rs. 2,500 which will be paid from out of the discount of Rs. 10,000. The balance Rs. 7,500 which is foregone as discount by the successful bidder will be distributed as dividend equally among all the 50 subscribers i.e., each subscriber would get a dividend of Rs. 150. Even the successful bidder would be earning this dividend of Rs. 150. All the members of the chit group would contribute their monthly subscription of Rs. 1,000 after deducting the dividend earned of Rs. 150 ie, they would be paying Rs. 850 only during that particular month. Similarly, any number of chit groups with variations are floated by the promoter company. The assessee-company can also become a subscriber. The company which promotes these chit groups compulsorily joins each and every group as one of the subscribers (as a foreman). At times it can subscribe to more than one chit in a group. This may become necessary due to business expediency i.e., if the required number of subscribers do not enroll to a particular chit group, the company many a times fills in this gap. At times, the company also steps in as a subscriber in cases where certain chit subscribers drop out or discontinue the subscription. There is no bar as to the number of chits a person can subscribe to."

2.5 From the above it is clear that a subscriber of chits when bid for a chit on discount such discount suffered by such subscriber, subject to 5% of subscription money payable to foreman Shriram Chits (P) Ltd under the provisions of Act, is distributor by way of dividend amongst all the subscribers. Thus discount suffered by the appellant is not a payment to Shriram Chits Pvt. Ltd., and hence the provisions of sec. 40A(2) are inapplicable. It is also submitted that Shriram Chits (M) Ltd., is not a concern falling under the provision of Sec.40A(2). Payment of 5% of subscribed amount payable, as per provision of law, can not be said to be unreasonable or high, which is only a part of discount. Discount is appropriated for distribution of dividend amongst the subscribers and not a payment to Shriram Chits. Such discount suffered is allowable business deduction as per above. decisions. Fact of subscription of various chits by appellant is evidenced by the fact that all chits subscribed are as floated by

Shriram Chits under duly registered schemes floated and registered under the provisions of The Chit Funds Act 1982, all chit agreements are duly registered, transaction are duly recorded in audited books of accounts and sufficient details, as referred above were submitted during assessment proceedings."

9. After considering the detailed submissions of the assessee, Ld.CIT(A) deleted the addition made by the Assessing Officer with the following observations: -

"5.1.2 Ground No. 2 to 5 are raised against the disallowance of discount of Rs.9,08,58,239/- made by A O. The Assessing Officer observed that Appellant company failed to furnish evidences, in spite of repeated opportunities, with regard to the investments in various chits and discount debited on prizing chits as claimed in Profit & Loss A/c whether pertain to financial year 2012-13. I have considered the facts as placed by the AO as well as submissions made by the Ld AR before me in written as well as oral submission.

5.1.2.1 The Ld AR drew my attention to the submissions made before AO, during assessment proceeding. In response to notice u/s 142(1) dated 21st July 2015, appellant under its submission dated 7th August, 2015 submitted a detailed note as to nature of its Chit business. It explained chit operation by an example as 40 persons participate for 40 months by contributing Rs. 250/- per month, per month collection be Rs 10,000/- each month an auction be conducted and every subscriber is entitled to offer a discount to bid amount collected. Out of discount foreman will get 5% of monthly collection and balance discount be distributed amongst the subscribers as dividend. The Provisions of Maharashtra Chit Fund Act 1974 and Chit Fund Act 1982 are referred and chit agreements are entered with Chit Co in terms of these acts. Any payment to an associate concern u/s 40A(2)(b) is denied.

5.1.2.2 Vide submission dtd. 12/01/16, the appellant filed a note on un-matured discount on Chits. It is stated that following the method of accounting as approved by AO in A.Y, 2003-04, discount is apportioned over the chit period and discount relating to current financial year period is claimed as allowable discount in current financial year and balance is claimed in subsequent years in which the period fall. It is explained by way of illustration. Further, vide letter dtd 27/01/16, appellant submitted (1) chit wise details of chits

in operation of Rs.67,81,20,200/-, subscription paid thereon Rs.41,52,95,370/- and subscription payable as on 31/03/2013 of Rs.26,28,24,830/ (ii) list of dividend received chit wise of dividend received Rs.5,60,85,485/- and (iii) details of unabsorbed discount chit wise of Rs.9,56,80,648/-. In response to notice u/s 142(1) dtd.23/01/16, the appellant filed details under its letter dated 05/02/16 of long term liability as trade payable, such liabilities were payable to M/s. Shriram Chits (Maharashtra) Ltd. It also filed details of un- matured discount of Rs.9,56,80,648/- which relates to F.YS. 2009-10 to 2012-13, it explained all the chit fund transactions carried with M/s. Shriram Chits (Maharashtra) Ltd. The procedure adopted for claiming discount on chits was explained.

5.1.2.3 I have considered the details submitted by appellant during the course of assessment proceedings and have also considered the submission of Ld. AR. during the course of appellate proceedings that all the transactions of chit subscription is carried out with M/s. Shriram Chits (Maharashtra) Ltd... The transactions are duly recorded under audited books of account, all the transactions are carried out through banking channel and all the details called for were submitted. Under the provision of Chit Fund Act, the agreement for each chit is required to be entered and registered, a few sample copies of chits agreements are submitted. I have perused details submitted, appellant having filled chit wise details of chit subscribed, chit wise dividend received along with other details, fact of subscribing chits with M/S Shriram Chits (Maharashtra) Ltd cannot be denied. The appellant explained method of write off of discount suffered on bidding on chits Discount is suffered in bidding process as prescribed under the provisions of Chit Act. I have considered the appellant's submission that it has not claimed whole of the discount in the year in which discount is suffered but it has claimed on proportionate basis having regard to period chit.

5.1.2.4 In case of Bilahari Investment (P) Ltd 299 ITR 1 (SC), observed: "Chit funds are basically saving schemes in which certain number of subscribers join together and each contributes a certain fixed sum each month, the total number of months being equal to the total number of subscribers. The subscriptions are paid to the manager of the fund by a certain prescribed date each month and the total subscriptions to the fund are auctioned each month amongst the subscribers. At each auction, the lowest bidder is paid the amount of his bid and the balance received from out of the total subscriptions received is distributed equally amongst other subscribers, as premium. The manager is paid a certain percentage of the collections each month on account of expenses and charges for conducting the auction. In the auction, a maximum amount,

which the highest bidder agrees to forego. is the amount, which is distributed to the other members, subject to deduction of the manager's commission. The Court held that claim of the discount is allowable as business expense and dividend received on chits is taxable as business income" In the case of Bilahari, whole of discount was claimed in the year in which chit was discounted, based on complete contract method, department allowed discount on proportionate period method. The Hon'ble Apex Court held that discount as allowable in the year in which it is incurred. Appellant in present case, following method approved by AO in A.Y. 2003-04 claimed discount as deduction on proportionate period basis, total discount suffered for the year is Rs. 10,80,03,880/-, discount claimed on proportionate period basis, Rs.5,36,72,780/- and balance discount claimed is discount suffered on chits discounted in earlier years for the period falling in current year. The appellant having consistently following same method discount claimed Rs.9,56,80,648/- relates to current financial year.

5.1.2.5 The Ld. DR has drawn my attention towards certain provisions of Chit Fund Act, 1982

(1) The following terms are defined u/s 2 of the said Act:

(c) "chit agreement" means the document containing the articles of agreement between the foreman and the subscribers relating to the chit,

(g) "discount" means the sum of money or the quantity of grain which a prized subscriber is, under the terms of the chit agreement, required to forego and which is set apart under the said agreement to meet the expenses of running the chit or for distribution among the subscribers or for both;

(h) "dividend" means the share of the subscriber in the amount of discount available under the chit agreement for rateable distribution among the subscribers at each instalment of the chit;

(j) "foreman" means the person who under the chit agreement is responsible for the conduct of the chit and includes any person discharging the functions of the foreman under section 39;

(m) "prize amount" means the difference between the chit amount and the discount, and in the case of a fraction of a ticket means the difference between the chit amount

and the discount proportionate to the fraction of the ticket, and when the prize amount is payable otherwise than in cash, the value of the prizes amount shall be the value at the time when it becomes payable;

(n) "prized subscriber" means a subscriber who has either received or is entitled to receive the prize amount;

5.1.2.6 In this case Shriram Chits (Maharashtra) Ltd is Foreman, it has to enter in agreements with each subscriber for each chit, under sec 4 state government permission is required to commence a chit, under sec 6 every chit agreement shall be in duplicate and shall be signed by each of the subscribers and the foreman and attested by at least two witnesses the probable date of commencement and the duration of the chit, it will contain prescribed particulars; duration of a chit shall not extend beyond a period of five years from the date of its commencement, the amount of discount referred to in clause (f) of sub-section (1) shall not exceed '[thirty per cent.]' of the chit amount, where the prized subscriber at any installment of the chit is required to be determined by auction and more than one person offer the maximum discount, the prized subscriber shall be determined by lot. As per sec every chit agreement shall be filed in duplicate by the foreman with the Registrar who will register the same. Under sec21 the foreman shall be entitled to such amount not exceeding five per cent. of the chit amount as may be fixed in the chit agreement, by way of commission, remuneration or for meeting the expenses of running the chits to receive and realize all subscriptions from the subscribers and to distribute the prize amounts to the prized subscribers; to demand sufficient security from any prized subscriber for the due payment of future subscriptions payable by him. Sec. 31 provides that every prized subscriber shall, if he has not offered to deduct the amount of all future subscriptions from the prize amount due to him, furnish, and a foreman shall take, sufficient security for the due payment of all future subscriptions. Every prized subscriber shall pay his subscriptions regularly on the dates and times and at the place mentioned in the chit agreement and, on his failure to do so, he shall be liable to make a consolidated payment of all the future subscriptions forthwith.

5.1.2.7 Discount suffered in bidding for chit is used, subject to 5% payable to foreman Shriram Chits (P) Ltd as per provisions of Act, for distribution by way of dividend amongst all the subscribers. Thus discount suffered by the appellant is not a payment to Shriram Chits (Maharashtra) Ltd, payment of 5% to Shriram Chits is as per

provisions of Chit Act, hence cannot be treated as excessive or unreasonable Hence, provision u/s.40A(2)(b) are not applicable.

5.1.2.8 In view of the discount borne by the appellant amounting to Rs 9,08,58,2396- is allowed as deduction. Accordingly these grounds are allowed.

5.1.3 Ground No.6 relates to addition made of Rs. 36,63,929/- to the income of the appellant The AO has held in para 5 of the assessment order, that month wise breakup of bidding of chits giving the particulars (1) Bid Amount (i) Prize Money on the chits (iii) Subscription arrear (iv) Current Sub & VC charges (v)Service Tax, were filled The AO held that appellant received Rs.5,97,49,414/- is income of the appellant, appellant having shown receipt of Rs.5,60,85,485/- the balance amount of Rs.36.63,929/- was added to the Income of the appellant. The similar issue was considered by CIT(A) in its appellate order for A.Y.2012-13 being ITA No.CIT(A)-24/ACIT-15(1)(2)/IT- 91/2015-16 dtd.30/05/16 wherein after considering the order of ITAT in case of Bilahari Investment (P) Ltd 299 ITR 1 (SC), and provision of section 32 of Chit Fund Act as per which a subscriber after getting the bid, is liable to make subscription for subsequent installments on chits, the amount received by the prized subscriber is not of the nature of income. The CIT(A) observed in appellate order for AY 12-13:

"Moreover, as pointed out by the Ld. AR, the Ld. AO has completely misunderstood the method of accounting followed and the nature of receipts and payments by wrongly holding that the receipts of the appellant company on account of bidding chits (net of expenses) was Net Profit. The fact remains that such a receipt was actually a Balance Sheet item which was appellant's liability and which by no stretch of imagination could be held as appellant's Net Profit. It is, therefore, held that the Ld. AO had misdirected himself in construing that the Balance Sheet item of liability which was to be paid by the appellant over the life of a chit was actually the appellant's income. The amount of Rs.4.12 crore shown by the appellant as total receipt was actually the dividend income which alone is liable to be taxed and regarding which Ld. AO has not raised any objection. Accordingly, grounds raised have to be allowed in favour of the appellant."

Respectfully following the above, the ground is allowed."

10. Aggrieved revenue is in appeal but raising following grounds in its appeal: -

"On the facts and in the circumstances of the case and in law, the Ld. CIT(A), erred in deleting the addition made by the assessing officer in respect of discounting of chit fund amounting to Rs.9,08,58,239/-, without appreciating that the assessee company has not brought any evidence on record to show that they have invested in a number of chits and has incurred such a huge discount."

2. *On the facts and in the circumstances of the case and in law, the Ld. CIT(A) erred in deleting the addition made by the Assessing Officer in respect of discounting of chit fund amounting to Rs.9,08,58,239/-, without considering the decision of Hon'ble Kerala High Court in the case of Ram Bahadur Thakur Ltd., 261 ITR 390 wherein it is held that when the claims are based on facts within the exclusive knowledge of the assessee, the assessee, has to place all facts and circumstances before the Revenue Authorities and the later must examine these and make up its mind as to whether the expenditure was justified by commercial expediency."*

3. *"The appellant prays that the order of the Ld.CIT(A) on the above directions be set-aside and that of the assessing officer be restored."*

4. *"The appellant craves leave to add or alter any of the aforesaid grounds or add a new ground of appeal, which may be necessary, at any time before or at the time of hearing of appeal".*

11. At the time of hearing, Ld. DR made her detailed submissions and also filed written submissions, the same is reproduced below: -

"Brief Points by Revenue.

- *The order of the AD is relied upon.*
- *Short note on the functioning of Chit Funds:*

A Chit fund is a rotating saving scheme that has been a part of India's Financial System for more than a century. In a chit fund scheme a group of people contribute periodically towards the chit value for a duration equal to the number of investors (members or subscribers)

The amount collected is given to the person, who is either selected through a lucky draw (lottery system) or an auction.

In the auction allotment system, the person who bids the lowest bid (agrees to claim the lowest amount) gets the money. This type of auction system is known as a reverse auction. The amount foregone by the winning bidder is then distributed among the other members equally after deduction the foreman's commission and other charges. The amount received by each member is called a dividend. Even after claiming the amount, the winning bidder has to continue investing.

The chit fund begins at the pre-decided date for the number of months equal to the number of investors. The subscribers contribute their monthly instalments into the pot. An open auction is then conducted, allowing the members to bid for the chit fund value. The subscriber who is willing to take the lowest sum is announced the winner and gets to take the chit fund for that month.

The math behind chit fund reverse auction scheme: Example

Let's assume that a chit fund scheme has 50 members, each paying a monthly instalment of Rs. 1000/- to have a first month pot of Rs. 50,000/- When the auction is announced, the member who bids to take home the least amount of the chit fund wins the bid. Lets assume that the winning bidder agrees to accept Rs. 45,000/- of the total chit fund value for that month, the discounted amount of Rs. 5000/- is distributed equally amongst the other 49 members after subtracting the organizer's fees: Highlights:

i) The winning bidder gets access to a lump sum of Rs.45,000/- in the first month.

(chit fund acts as a borrowing scheme here)

ii) The other 49 members earn good returns on the amount they invested. (Chit fund acts as a savings instrument here)

iii) The organizer gets the commission

Chit fund allows the organizer to be compensated for putting in efforts to organize the event.

A win-win situation for all.

Features of Chit Funds:

a) They are a credit and savings schemes rolled into one

- b) *Act as a micro finance institution*
- c) *Have a predetermined value and duration.*
- d) *Allow you to borrow at an interest rate lower than money lenders.*
- e) *Best for meeting the financial requirements of people belonging to lower income households.*
- f) *Deposits made by all the subscribers are turned into a lump sum.*

Benefits of Chit Funds:

1. *A saving and investment tool-Advantage of saving as well as borrowing*
2. *Quick access to money. Easy to join and opportunity to borrow the lump sum by paying just the first instalment.*
3. *Very little paper work.*
4. *No collateral Unlike banks or other financial institutions - No tangible security required.*
5. *No need to reveal the purpose of using the borrowed money.*
6. *Emergency-Easily access during an emergency*
7. *High Dividend: The subscribers get a dividend which is comparatively higher than the interest accrued on the money saved in various deposit schemes*
8. *Low Interest: The subscribers mutually determine the interest rate, and it varies from auction to auction. The interest rate of borrowing from the chit fund is comparatively lower than other forms of borrowing.*

Comments : If the chit fund scheme is studied carefully, the discounted chit proceeds is divided among all the members and the assessee also gets his share of the prize money or discounted amount. Similarly in the next month, another person will be discounting and taking the amount. Depending on the need of the person winning the auction, the discounted amount can be higher or lower. This amount discounted is also divided amongst all and this

process continues. Hence, in fact, even if Assessee has discounted his chit in the first month itself, the actual loss incurred is reduced and at the end he actually stands to gain a profit. In this business the profit varies between 10% to 12%. The claim of the Assessee that he has incurred heavy losses is not tenable for the following reasons:

1) No prudent businessman will continue to invest in Chit Funds every year, if he is incurring heavy losses. The question arises, that despite losses how is he able to finance the instalments of the chits.

2) The argument of the Assessee that the same is out of dividend and interest received from the chit company is not acceptable because he has shown a very meagre amount in comparison to the amount he has to invest or pay as monthly instalments

The Assessee may be requested to file a monthly fund flow statement in respect of each chit that the Assessee has purchased/joined.

3) In the market the profit trend is 10%-12% to the subscribers of Chit Funds.

4) Every Chit has a pre-determined value and duration. If the Assessee is incurring losses that he can stop repeated investment in new chits.

5) Another question that arises is if he is incurring heavy losses due to chit discounting what is inducing the Assessee to continue to invest more and more in new Chits in the same Chit Fund Company?

6) It may also be noted that the Assessee Company has a paid up capital of Rs. 10 lakhs only.

7) Share Holdings: Page 8 of Paper Book

<i>a) Shriram Investments</i>	<i>10%</i>
<i>b) Shriram Construction Finance</i>	<i>10%</i>
<i>c) Shriram Capital Trust Pvt Ltd held on behalf of Shriram Corporation Leasing</i>	<i>10%</i>
<i>d) Shriram Professional Finance</i>	<i>10%</i>
<i>e) Shriram Office Equipment Leasing</i>	<i>10%</i>
<i>f) Shriram Shriram Finance</i>	<i>10%</i>
<i>g) Shriram Capital Trust Pvt Ltd held on behalf of Shriram Domestic Finance</i>	<i>10%</i>

<i>h) Shriram Consumer Durable Leasing</i>	10%
<i>i) Shriram Medical Equipment Finance</i>	10%

It may be noted that the major share holders of Assessee Company are group companies of Shriram Chit Funds (Maharashtra) Ltd as is evident from the above. Further, on perusal of page 37 of Assessee's paperbook, it is evident that the shareholders of M/s Shriram Chit Funds (Maharashtra) Ltd also has its group companies and directors as shareholders. The entire set up is only a ploy by the assessee company to offset the losses of Shriram Chit Funds (Maharashtra) Ltd and in actuality, there are no bill discounting losses incurred by the assessee company. It is reiterated that no prudent businessman will continue to incur losses year after year and persistently invest in chits with the same Chit Fund company.

Attention is drawn to page no.. 39 of Assessee's paper book wherein details of Chit discount claimed and as per amount worked out by AO. It is apparent that the Assessee is inflating the chit discounting amounts and claiming huge losses.

In accordance with the Madras Chit Fund Act, 1961 and Delhi Chit Fund Rules, 1964, no person shall start or conduct any chit or publish any notice, circular, prospectus or other documents containing the terms and conditions of any chit, or inviting the public to subscribe for tickets in any chit, the bye-laws of which have not been registered. In accordance with Section 7 of the Madras Chit Fund Act, 1961 as extended to NCT of Delhi, "No person shall commence any auction or draw of any chit unless he has obtained a certificate of commencement from the Registrar, Chit Funds". Whenever you wish to start a new chit group, you have to get bye-laws for that particular chit group registered with the Registrar, Chit Funds. After the Bye-laws of a chit group are approved by the Registrar, Chit Funds and the company wishes to start the particular chit group, they have to keep in mind the following things before enrolment of subscribers:-

- 1. All subscribers should be adults.*
- 2. All subscribers must be having their regular source of income.*
- 3. In case of a Company applying for a subscription, it shall subscribe for only one ticket in one particular group.*
- 4. No person can subscribe normally for more than two tickets in one particular group.*

5. If any subscriber is related to any Director of the company, the information should be given to the Registrar Chit Fund in Circular No. 11.

Further, the revenue also relies on the decision of the Hon'ble Kerala High Court in the case of Ram Bahadur Thakur Ltd 263 ITR 390, wherein it is held that when the claims are based on facts within the exclusive knowledge of the assessee, the assessee, has to place all facts and circumstances before the Revenue Authorities and the latter must examine these and make up its mind as to whether the expenditure was justified by commercial expediency. (Copy attached)

12. On the other hand, Ld. AR Shri Shivram, Advocate appeared on behalf of the assessee and brought to our notice the Chit Funds Act, 1982 which is placed on record in Page No. 1 to 61 of the Paper Book and further, he submitted that the grievance of the revenue is that assessee has not submitted any document before the Assessing Officer. However, he submitted that the assessee has submitted all the relevant documents before the Ld.CIT(A) who has coterminous power to accept the various documents which has not been submitted before the Assessing Officer. Ld. AR submitted that the grievance of the Assessing Officer is already addressed by the assessee and this is not the first year of assessment, the assessee is being assessed from the A.Y. 2003-04 onwards and he submitted that the details of returns filed by the assessee till A.Y.2021-2022 and the details are placed at Page No. 62 of the Paper Book. Referring to the profit or loss declared by the assessee, objecting to the submissions

made by the Ld.DR that assessee is bidding for the chit funds and offers a discount and such discounts are not charged to the Profit and Loss Account on the year of offering the discount. He brought to our notice decision of the Bilahari Investments (P.) Ltd. *v.* CIT [2007] 164 taxman 443 (Madras) and he brought to our notice Page No. 146 of the Paper Book in which the Hon'ble Madras High Court had held that the discount was not a deferred expenditure for which payment has been made or a liability incurred, but the discount was carried forward on the presumption that it will be of benefit over a specific period. It was observed that in the chit transaction, there was no deferred benefit, which was construed to mean the benefit deferred to a year subsequent to the accounting year and hence the question of deferred expenditure did not arise. That means Hon'ble Madras High Court directed the assessee to book the discounts in the year in which the payment was made or offered.

13. He Further, submitted that the above decision was also upheld by the Hon'ble Supreme Court, copy of same is placed in Page No. 155 of the Paper Book. However, he submitted that the assessee was consistently following the method of recording the discount as per the direction given by the Assessing Officer in A.Y. 2002-03 which was

consistently followed by the assessee. Therefore, assessee offers the discount relating to the current period and other discount which is not related are carried forward. Similarly, the discount offered during the year are also treated the same way and to the extent relevant for the present period are shown as expenditure and balance for the relevant future period was carried forward.

14. He brought to our notice the statement of chit loss account for the F.Y. 2012-13 which is placed at Page No. 85 of the Paper Book which is the amount allocated for the current year and carried for the future years beyond 31.03.2013 and the above statement contains the details of chit value, branch name and operation of the chit, start and end date of the chit and the discount foregone in each chit along with the allocation and similar chit loss account for the F.Y. 2013-14 also placed on record at Page No. 127 of the Paper Book.

15. With the above submissions, Ld. AR submitted that the grievance of the revenue is already addressed by submitting all the relevant information before the Ld.CIT(A) as well as before Hon'ble ITAT. He heavily relied on the decision of the Bilahari Investments (P.) Ltd. v. CIT

(supra) which is binding ratio in the case of assessee and he submitted that the revenue is consistently raising this issue over the years and the issues raised by the revenue are already considered and decided in favour of the assessee by First Appellate Authority. He prayed that order of the First Appellate Authority be confirmed.

16. Considered the rival submissions and material placed on record, we observe from the submissions of the Ld.DR which are similar to the observations of the Assessing Officer and further, Ld.DR also highlighted the unreasonableness conduct of the assessee and no prudent businessmen will incur such losses and further, she submitted that assessee is one of the group concern of Shriram Chit Funds (Maharashtra) Ltd., Further, she submitted that the whole setup is only a ploy by the assessee to offset the losses of Shriram Chit funds (Maharashtra) Ltd.,. After considering the submissions of the Ld.DR as well as counsel for the assessee we observe that the business of the assessee is subscriber to the chit funds and it regularly subscribes to the chits floated by SCML and it maintains the total record of the chits bid by them and discount offered to bid the chit by them over the years and it follows a consistent method of allocating the discount over the period of chit related to the various

chits bid by them. The statement clearly indicates that assessee follows the consistent method of allocation and it has submitted the chit wise details before the Ld.CIT(A) and Ld.CIT(A) considered the submissions in detail and he is of the opinion that all the details submitted by the assessee are consistent with the method of account applied by them. We observe that assessee is consistently following the same method of account and declares the income and expenditure consistently following the same. On a careful reading of the decision of the Hon'ble Madras High Court in the case of Bilahari Investment (P.) Ltd. v. CIT (supra) which was upheld by Hon'ble Supreme Court that the chit is a kind of saving scheme and the various modes of operation adopted and recorded by chit bidder and chit companies, for the sake of clarity, the findings of the Hon'ble Madras High Court decision are reproduced below: -

"19. When the chit is auctioned every month, the bidder takes the chit for an amount which is less than the face value of the chit. The difference between the face value and the auctioned value during every month is the gross dividend generated in that month. This amount of dividend gets distributed among all the members (subscribers) equally. The members (subscribers) need not pay the total monthly subscription and instead, they have to pay the monthly subscription after deducting the amount of dividend earned. The members who have taken the chit in auction have the ability to keep the contribution to the chit till the end of the chit period and the prized members would be getting dividend in future months also. Insofar as the discount, namely, the difference between the face Value of the chit amount and the auctioned amount is concerned,

the assessees have considered it as their bid loss and claimed the same as allowable during the year in which it occurred.

20 *In this view of the matter, when the Revenue claimed the dividend as taxable in the relevant accounting year, the assessees claimed that the dividend is taxable only on the completion of the chit period. Similarly, while the Revenue claimed that the discount is allowable as business loss proportionately, the assessees claimed that the discount is allowable in the same accounting year in which it occurred.*

21. *The Andhra Pradesh High Court in CIT v. Kovur Textiles & Co.[1982] 136 ITR 61 found that the assessee- company subscribed to a chit fund by joining in a chit group and after paying a few instalments, the assessee bid the chit and claimed the difference between the chit amount and the price for which it was bid as a business loss. On the factual backdrop, the Andhra Pradesh High Court held that the loss incurred by the assessee in the process of bidding the chit amount could be allowed as a business loss.*

22. *Of course, the Punjab and Haryana High Court in Soda Silicate & Chemical Works v. CIT[1989] 179 ITR 588 took a contra view that where the assessee secured a chit on discount and claimed deduction of discount amount while computing its assessable income, the loss incurred thereon was not incidental to the business and therefore, disallowed the assessee's claim during the year in question.*

23. *We are unable to agree with the decision of the Division Bench of the Punjab and Haryana High Court in Soda Silicate & Chemical Works' case (supra). The Punjab and Haryana High Court held that the discount amount is not allowable as business loss on the ground that the transaction involved did not give rise to any income assessable to income-tax, nor any revenue loss in respect of which any deduction could be claimed. The judgment of the Punjab and Haryana High Court has no relevance to the facts of the present case, as, in this case, business loss occurred during the previous year relevant for the assessment year and the discount is found to be connected with the business activities of the assessees, whereas in the case before the Punjab and Haryana High Court, on facts, it was found that the discount is not connected with the business of the assessee. On the other hand, the facts of the present case are similar to that of the case before the Andhra Pradesh High Court, viz, Kovur Textiles & Co.'s case (supra) and hence, we agree with the view taken by the Andhra Pradesh High Court*

24. *The Tribunal relied on the decision of the Supreme Court in Madras Industrial Investment Corpn. Ltd.'s case (supra) and held*

that the dividend is taxable and discount is allowable both during the accounting year proportionately. In Madras Industrial Investment Corpn. Ltd's case (supra), the assessee-company issued debentures at a discount and it incurred a liability to pay a larger amount than what it had borrowed. The liability to pay the discounted amount over and above the amount received for the debentures is a liability which has been incurred by the company for the purposes of its business in order to generate funds for its business activities. Then, while deciding the question whether such a liability is an expenditure or not, the Apex Court held that the liability to pay discounted amount over and above the amount received for the debentures is a liability incurred by the company for the purposes of its business in order to generate funds for its business activities and therefore, It is an expenditure. The Apex Court also held that it is an expenditure deductible only proportionately during the period of assessment years.

25. The decision of the Apex Court in Madras Industrial Investment Corpn. Ltd's case (supra), as rightly pointed out by learned counsel for the appellants/assesseees, is distinguishable on the facts of the case.

26. The present case relates to the chit fund transaction. The chit is a kind of savings scheme. In a chit scheme, a C specific number of individuals come together to pool a specific amount at periodic intervals. Usually, the number of individuals and the number of periods will be the same. At the end of each period, there will be an auction of the money. The members of the chit will participate in this auction for the pooled money during that interval. The bid amount will be divided by the number of members and thus determining per head contribution during that period. Usually the discount, namely, the sum of money which the prized subscriber is required to forgo, will continue to decrease over periods. The person getting money in the last period will receive the full scheme amount.

27. On the other hand, the debenture is an instrument of debt executed by the company acknowledging its receipt to repay the same at a specified rate and also carrying interest. It is in sum and substance a certificate of loan or a bond evidencing the fact that the company is liable to pay a specified amount with interest. A debenture is unsecured in the sense that there are no liens or pledges on specific assets. It is, however, secured by all properties not otherwise pledged. In the case of bankruptcy the debenture holders are considered general creditors. When a company issues debentures at a discount, the debenture holders are required to pay a lesser sum than the face value and the company incurs a liability

to pay a larger amount than what it has borrowed, at a future date. The liability to pay the discounted amount over and above the amount received for the debentures is a liability which has been incurred by the company for the purposes of its business in order to generate funds for its business activities.

28. Insofar as debenture is concerned, the benefit to be derived from the amount borrowed will continue till the debenture is redeemed and the liability is a continuing liability which should be spread over the period of the debentures. But, in a chit transaction, a member of the chit will forgo the discount when he bids the chit. The discount amount varies in each period and it has no connection or relevance to the liability to pay future instalments. In other words, in a chit transaction the discount is based on the bid and the bid loss has no relevance to the liability for future instalments, whereas in the case of discount on debentures, it is not based on any bid loss, but it spreads over the period of life of the debentures. In the case of debentures, it is a case of receipt, while In the case of chit transaction, it is an amount paid followed by the encashment of the chit amount at an early date with the promise to pay the remaining instalments. In this view of the matter, the decision of the Apex Court in Madras Industrial Investment Corpn. Ltd.'s case (supra) is not applicable as in the instant case the discount arises out of a chit transaction, whereas the Apex Court dealt with the discount on the issue of debenture.

29. A five-Judge Bench of the Kerala High Court in Janardhana Mallan v. Gangadharan [1985] 58 Comp. Cas. 390 held that on entering into the chitty agreement a debt is not incurred by the subscriber for the amount of all the future instalments, but it is a promise to discharge the contractual obligation, whether the prize is drawn or not or the prize amount is received or not. It is also held that but for such obligation there will be no difference between the liability of the prized subscriber and the non-prized subscriber and both arise out of the same contract and that since both profit and loss arise simultaneously on the date of prize drawn itself, the question of incurring fresh obligation to pay future subscription does not arise. Therefore, the subscriber is entitled to deduction of discount as business loss in the accounting year in which it occurred.

30. As observed earlier, in the chit transaction there is only a promise on the part of the assesseees to discharge the contractual obligation. Further, the assessee companies following the mercantile system of accounting as statutorily required under the Companies Act, have to account for their income or loss as per the mercantile system of accounting and not otherwise. In other words, the income

or loss of the assessee accruing during the relevant accounting year has to be considered for the purpose of income-tax assessment. When the assessee is in the business of subscribing to chits and deriving income out of it during a particular year, it is not possible or permissible to defer its assessability till the completion of the entire cycle of the chit.

31. *At this juncture, it is apt to refer to sections 5 and 145 of the Income-tax Act:*

"5. Scope of total income-(1) Subject to the provisions of this Act, the total income of any previous year of a person who is a resident includes all income from whatever source derived which-

(a) is received or is deemed to be received in India in such year by or on behalf of such person; or

(b) accrues or arises or is deemed to accrue or arise to him in India during such year; or

(c) accrues or arises to him outside India during such year:

Provided that, in the case of a person not ordinarily resident in India within the meaning of sub-section (6) of section 6, the income which accrues or arises to him outside India shall not be so included unless it is derived from a business controlled in or a profession set up in India.

(2) Subject to the provisions of this Act, the total income of any previous year of a person who is a non-resident includes all income from whatever source derived which-

(a) is received or is deemed to be received in India in such year by or on behalf of such person; or

(b) accrues or arises or is deemed to accrue or arise to him in India during such year.

Explanation 1.-Income accruing or arising outside India shall not be deemed to be received in India within the meaning of this section by reason only of the fact that it is taken into account in a balance sheet prepared in India.

Explanation 2-For the removal of doubts, it is hereby declared that income which has been included in the total income of a person on the basis that it has accrued or

arisen or is deemed to have accrued or arisen to him shall not again be so included on the basis that it is received or deemed to be received by him in India"

145. Method of accounting (1) Income chargeable under the head Profits and gains of business or profession or Income from other sources shall, subject to the provisions of sub-section (2), be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee.

(2) The Central Government may notify in the Official Gazette from time to time accounting standards to be followed by any class of assessee or in respect of any class of income.

(3) Where the Assessing Officer is not satisfied about the correctness or completeness of the accounts of the assessee, or where the method of accounting provided in sub-section (1) or accounting standards as notified under sub-section (2), have not been regularly followed by the assessee, the Assessing Officer may make an assessment in the manner provided in section 144."

32. A conjoint reading of the above provisions of law makes it clear that all income received or deemed to be received or accruing or arising during the previous year shall form part of the total income of the assessee and such income shall be computed in accordance with the accounting system which the assessee is regularly following. Here, on the facts of the case, the authorities have found that the assessee is following the mercantile system of accounting. The mercantile system of accounting means, as discussed in Shiva Prasad Gupta v. CIT AIR 1929 All 819, the amounts that have become recoverable are shown as the income actually received and the liabilities incurred are shown as amounts actually disbursed in any particular year. Therefore, when the assessee is following the mercantile system of accounting, in which entries are posted in the books of account on the date of the transaction, that is, on the date on which rights accrue or liabilities are incurred irrespective of the date of payment, they have to account for their income or loss as per the mercantile system of accounting and not otherwise. Therefore, as rightly found by the Commissioner of Income-tax (Appeals), the income derived during a particular previous year by way of chit dividend has to be reckoned and assessed as income of that year following the principles of mercantile accrual system of

accounting, particularly when the assesseees are companies following the mercantile system of accounting.

33. The chit transaction is governed by the provisions of the Chit Funds Act. In view of the non obstante clause found in section 3 of the Chit Funds Act, 1982, namely,

*3. Act to override other laws, memorandum, articles, etc. -
 Save as otherwise expressly provided in this*

(a) the provisions of this Act shall have effect notwithstanding anything to the contrary contained in any other law for the time being in force or in the memorandum or articles of association or bye-laws or in any agreement or resolution whether the same be registered, executed or passed, as the case may be, before or after the commencement of this Act, and

(b) any provision contained in the memorandum, articles, bye-laws, agreement or resolution aforesaid, shall, to the extent to which it is repugnant to the provisions of this Act, become or be void, as the case may be."

the definitions of the expressions, 'discount', 'dividend', 'prize amount, as extracted above, will prevail over the similar definitions as found in the Income-tax Act, because a non obstante clause is generally appended to a section with a view to give the enacting part of the section in case of conflict, an overriding effect over the provision in the same or other Act mentioned in the non obstante clause (vide: State of Bihar v. Bihar Rajyo MSESKE. Mahasangh [2005] 9 SCC 129. Therefore the discount is not an interest payable on the prized amount, but it is a loss.

34. As already observed, in chit transaction there is no correlation between the discount amount and the future instalments. Further, the measure of future instalments does not depend upon the prized amount or the discount, nor the discount is an expenditure to be incurred in future. The discount is not a deferred expenditure for which payment has been made, or a liability incurred, but the discount is carried forward on the presumption that it will be of

benefit over a specific period. In the chit transaction, there is no deferred benefit, which is construed to mean the benefit deferred to a year subsequent to the accounting year and hence, the question of deferred expenditure does not arise."

17. From the above it is clear that the various method of accounting of dividend/premium income, discount are discussed in detail. Therefore, the nature of transaction in chit fund is the subscriber takes the call to bid the discount to receive the total funds of the particular chit. In the given case assessee bids to offer the discount with its wisdom and takes the full funds for the respective chits subscribed during the year. The assessee commits to repay the balance installment of the various chits subscribed by the assessee. In this case, assessee has already deposited the balance installment to the foreman, in this case Shriram Chits (Maharashtra) Ltd., The whole business of subscribing to the chits are clearly recorded by the assessee and it is properly audited. Hence, the method adopted by the assessee is proper and the business carried on by the assessee is proper and within the four corners of the law. No doubt assessee records huge discount during the year which is based on the method adopted by the assessee to allocate the relevant period. It is a continuous process as the business of the assessee itself is to subscribe to the various chits. In the chit's business the discount offered and subsequent receipt of premiums

from the other subscriber's discount is integral part of the chit business. One cannot separate the same. The income from these transaction of subscription in the chit business is the difference between interest from deployment of funds, premium received and the discount offered for the chit during the year. The assessee has recorded properly the premium received and the discount pertaining to the impugned assessment year. It clearly shows as per the statement submitted by the assessee that assessee declared the profit in A.Y.2017-18, A.Y.2018-19 and A.Y. 2019-2020. Therefore, the revenue cannot see one particular year and come to the conclusion, in our view, they need to monitor the result over the period of time. Therefore, in our considered view the accrual system of accounting followed by the assessee which is as per the proved method of accounting and income and discount charged to the Profit and Loss Account are consistent with the method adopted over the period of time. Therefore, we do not see any unreasonableness in the method of accounting adopted by the assessee. The revenue is questioning the rationale of subscribing to the chits and taking the huge discount, in that process the assessee is incurring huge loss. Further, we observe that Assessing Officer has disallowed only the discount without looking at the nature of chit business. He has to see overall earnings or loss from the

peculiar transactions in the chit business. Therefore, we are inclined to agree with the findings of the Ld.CIT(A) and we do not see any reason to infer otherwise. Accordingly, grounds raised by the revenue are dismissed.

ITA.No. 3251/MUM/2019 (A.Y. 2014-15)

18. Coming to the appeal relating to A.Y. 2014-15, since facts in this case are mutatis mutandis, therefore the decision taken in A.Y. 2013-14 is applicable to this assessment year also. Accordingly, this appeal is dismissed.

19. To sum up, in the result, both the appeals filed by the Revenue are dismissed.

Order pronounced in the open court on 03rd March, 2023

Sd/-
(ABY T. VARKEY)
JUDICIAL MEMBER
Mumbai / Dated 03/03/2023
Giridhar, Sr.PS

Sd/-
(S. RIFAUH RAHMAN)
ACCOUNTANT MEMBER

Copy of the Order forwarded to:

1. The Assessee
2. The Respondent.
3. The CIT(A), Mumbai.
4. CIT
5. DR, ITAT, Mumbai
6. Guard file.

//True Copy//

BY ORDER

(Asstt. Registrar)
ITAT, Mum