

**IN THE INCOME TAX APPELLATE TRIBUNAL
“A” BENCH : BANGALORE**

**BEFORE SHRI N.V. VASUDEVAN, VICE PRESIDENT AND
SHRI B. R. BASKARAN, ACCOUNTANT MEMBER**

ITA Nos.1706 to 1708/Bang/2019
Assessment Years : 2015-16 to 2017-18

M/s. Gowrinath Chits Pvt. Ltd., 1178/1, 16 th Main Road, BTM Layout, Bengaluru – 560 068. PAN : AAFCG 5113 L	Vs.	ITO, Ward – 3(1)(2), Bengaluru.
APPELLANT		RESPONDENT

Assessee by	:	Shri. K. R. Vasudevan, Advocate
Revenue by	:	Shri. Sankar Ganesh K, JCIT(DR)(ITAT), Bengaluru.

Date of hearing	:	23.02.2022
Date of Pronouncement	:	25.02.2022

ORDER

Per N. V. Vasudevan, Vice President :

These are appeals by the assessee against three orders, 2 orders dated 10.06.2019 and one order dated 31.05.2019 of CIT(A) - 3, Bengaluru, in respect of Assessment Years 2015-16, 2016-17 and 2017-18.

2. The issue that arises for consideration in all these appeals is common and relates to the determination of income in the business of running chits. The assessee is a private limited company and was incorporated on 13.06.2014. The Financial Year relating to Assessment Year 2015-16 is the first year of operation of the assessee. The assessee as a foreman conducts several chit series and enrolls members to contribute to each chit series. The subscribers to the chit series have to contribute certain sum of money by way

of periodical instalments for a definite period. Each of the subscriber in chit series can bid by auction and obtain a specified sum as a prize money. The subscriber however will continue to contribute to the chit instalments for the duration of the chit series.

3. If the duration of the Chit is 50 Months then the term period of the Chit Group is 50 Months and Chit Fund Company has to gather 50 people who are interested in investing in this chit group. These 50 persons are called **Subscribers**. If the chit value is fixed as Rs.500000/- by the company the maximum monthly contribution payable by each subscriber will be Rs.10000/- (50 Nos x Rs.10000). This is also known as **Monthly Subscription**. It may be noted here that the number of persons investing in a chit and the duration of the chit is always the same.

4. The Subscriber does not always pay the entire Subscription amount every month. Suppose a subscriber had bid 35% of Rs.500000/- which is Rs.175000/- then this amount is known as **Chit Discount**. The foreman charges 5% of chit value as commission. In this illustration, that would amount to Rs.25,000/- This is deducted from Chit Discount i.e. $175,000 - 25,000 = 150,000$. This amount is available for equal distribution among the subscribers. 150,000 would be divided equally among 50 subscribers. Each subscriber would get a discount of $150,000/50 = 3000$. This amount is known as **Dividend**.

5. In the following month, all subscribers would have to only pay Rs.7,000 instead of Rs.10,000. This is because they have earned a chit discount of Rs.3000/-. Depending upon the competition within the chit group the discount percent would vary. The least discount would be 5% or less

which is the foreman's commission. The bidding process will continue until the end of the chit period.

6. During the previous year relevant to AY 2015-16, the assessee conducted the following chit groups with duration of 20 and 25 months and Chit values.

Chit Code	No of Monthly Instalment	Per Month Instalment Rs.	No of subscribers	Chit Value Rs.
GN2	20	2500	20	50000
GN2	20	5000	20	100000
GN2	20	10000	20	200000
GN2	20	15000	20	300000
GN2I	20	25000	20	500000
GN2J	20	50000	20	1000000
GN3	25	12000	25	300000
GN3	25	20000	25	500000

7. The assessee accounted for commission on the basis of commission accrued on the basis of percentage of completion method from each group for each financial year was as follows: -

Chit Group	No of Prized	Chit commission
GN2D	13	30000
GN2E	79	342500
GN2F	74	515000
GN2G	85	837500
GN2H	73	1125000
GN2J	35	1007500
GN3H	40	662500
TOTAL		4520000

8. A survey under section 133A of the Income Tax Act, 1961(Act) was conducted by the Revenue in the business premises of the assessee on 28.2.2018 to verify the business activities of the company. A statement under section 133A was obtained and which were signed by the authorised signatory. On the basis of the Statement made in the course of Survey u/s.133A of the Act, the revenue concluded that on the first instalment amount collected at the starting of a Chit Group from a chit subscriber commission is earned and received. As per the statement recorded at the time of survey total chit business in AY 2015-16 was Rs.24,51,00,000 and on that 5% commission was computed by the AO to arrive at a chit business commission income of Rs.1,22,55,000/-. The assessee had offered to tax a sum of Rs.45,20,000/- as commission income. Accordingly, an addition to the income to the tune of 7735000/- was made by the AO for AY 2015-16. Similar addition was made in the other two AYs also. The relevant part of the statement u/s.133A of the Act on the basis of which the assessment order was passed is as cited below:

Q14. Please furnish details of commission received financial year wise.

The information recorded under this question was value of the chit subscription enrolled for all chit groups financial year wise not the commission received financial year wise.

Q.15. Answer is that "Yes, 5% of the above business receipts (amounts recorded under question no.14) is the commission of the company for the respective financial years". In fact the amount recorded in Question No.I4 was neither "commission received" nor "business receipts" but it was value of chits enrolled by the subscribers of all groups.

133A statements are computer generated statements by the survey team which were later on got it signed from the authorised representative of the company present at the premises of survey.

9. The order of the AO was confirmed by the CIT(A) for all the three AYs, hence these appeals by the assessee before the Tribunal.

10. The learned counsel for the assessee submitted that there is no dispute between the revenue and the assessee on the quantum of business done by the assessee during all the three AYs and the dispute is only with regard to the time at which income from running of chits is to be recognized. In this regard, the learned counsel for the assessee drew our attention to the additional evidence filed by the assessee to demonstrate as to how the method of accounting adopted and estimation of income done by the Revenue is against the principles laid down by the Hon'ble Courts. The following additional evidence were filed before us as additional evidence:

PARTICULARS	PAGE NO
Summary of Chit - GN2H/15	001 - 002
Payment vouchers and pass-book of members	003 - 078
Summary of Chit - GN2H/17/BGL	079 - 080
Payment vouchers and pass-book of members	081 - 164
Summary of Chit - GN2H/07	165 - 166
Payment vouchers and pass-book of members	167 - 248

11. The learned counsel for the assessee submitted that the additional evidence gives details of three schemes, as an illustrative example, to demonstrate the method of accounting adopted and how estimation of income @ 5 % of chit collections is against the principles laid out by the Hon'ble Courts. It was submitted that the assessee runs many chit schemes at any point

of time and the details of each of these schemes are maintained meticulously in separate notebooks. The details of the schemes are extracted in the assessment orders. As can be seen from the additional evidence filed, each of the schemes run for 20 months. Therefore, the chit collections in a particular year will be from many such schemes and the end point of each of the schemes will be different and may fall in different years. In a chit scheme, a 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 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 forego, will continue to decrease over periods. The person getting money in the last period will receive the full scheme amount.

12. As regards the method of accounting to be adopted for chit fund schemes, The Hon'ble Madras High Court, in the case of Shriram Chits & Investments (P) Limited TCA No.141 of 2004 judgment dated 30.8.2012 had observed as under (**Para 13**) :

“Given the fact that each chit series is a transaction by itself, with intervening activities in the conduct of the chit transaction, with the conduct of the auction of every month facing ups and downs and ultimately seen in the matter of discount, the determination of the income of the assessee, thus, has to be necessarily postponed to the end of the transaction viz., end of the each series

....Hence, given the nature of the chit transaction with each series running through the number of months, the income arising out of the particular series of chit transaction could be identified only at the end of the transaction, which may consist of a series of activities and at any

intermediate stage of the chit transaction, there is no possibility of Identifying the income, but has to be postponed to the last performance. In the circumstances, the decision of the Apex Court in the case of CIT Vs. Bilahari Investment P. Ltd (cited supra) supports the case of the assessee that the income of the assessee on the dividend earned every month and the discounts arising therefrom have to be necessarily taken to the end of the chit period for the purpose of ascertaining the income.

Para-32: ...The Assessee is justified in following the mercantile system of accounting and adopting the completed contract method, to arrive at the real income. “

13. It was therefore submitted that the assessee is justified in following the mercantile system of accounting and adopting the completed contract method, to arrive at the real income. **As regards the claim of expenses**, the Hon'ble Court in the very same judgment had observed that,

“30.Taking note of the business of the assessee, we agree with the assessee's contention that the expenses cannot be viewed as relatable to the particular series alone, but as relating to the running of the business. Thus it has to be revenue expenditure to be considered in the year in which the same is incurred.

14. The learned counsel for the assessee therefore submitted that in view of the above, the method of estimation of income adopted by the AO, by estimating the income @ 5 % of the gross chit collections for the year is wrong. The correct method is to reckon the income for each of the chit schemes individually, at the end of the Chit period and the expenses to be recognised at the time of accrual. In this regard, he drew our attention to point No.2 "Revenue recognition" of Note No.1 of Significant "Accounting policies" of Audited financial statement of the assessee company which states that " **Revenue from services are recognised on completion of rendering services to the subscribers of the each chit groups by periodical auction and distribution of auction amount to prized bidder**". The commission

accrued on the basis of percentage of completion method and as per accounting policy of the company from all groups for the financial year (AY 2015-16) was Rs.4520000/- The Chit Company/ foreman allowed a five percentage as commission or remuneration at the time of each monthly draw and is permitted to pay himself from the subscription amount. Company's commission or remuneration that becomes due to him at that draw. Thus, remuneration or commission of the foreman accrues **at the end of chit** draw and it becomes due to him and is payable to him from out **of** the monthly subscriptions. The accrual of income as commission together with the right to receive it, **is related to each draw** and gets completed on that basis. Thus, **the** foreman's commission has to be related to and determined on the basis of every auction.Learned DR relied on the order of the AO/CIT(A).

15. We have considered the rival submissions. The additional evidence filed by the assessee demonstrates as to how the method of accounting adopted and estimation of income done by the Revenue is against the principles laid down by the Hon'ble Courts. In our view, for proper adjudication of the issue before the Tribunal, the following additional evidence which were filed before us as are admitted.

16. We are of the view that in the light of the additional evidence, the issue has to be set aside to the AO for consideration denovo. We may also add that the principles laid down in the decision of the Hon'ble Madras High Court and referred to in this order have also to be kept in mind by the AO in the set aside proceedings and the issue to be examined in the light of the additional evidence which demonstrates that the method of accounting followed by the assessee. The AO will afford opportunity of being heard to the assessee in the set aside proceedings. The facts in all the cases are identical and therefore we

have not discussed the factual details with regard to Assessment Year 2016-17 and 2017-18. We accordingly allow these appeals for statistical purposes.

17. In the result, all the appeals are allowed for statistical purposes.

Pronounced in the open court on the date mentioned on the caption page.

Sd/-

(B. R. BASKARAN)
Accountant Member

Bangalore.

Dated: .02.2022.

/NS/*

Sd/-

(N. V. VASUDEVAN)
Vice President

Copy to:

- | | |
|---------------|---------------|
| 1. Appellants | 2. Respondent |
| 3. CIT | 4. CIT(A) |
| 5. DR | 6. Guard file |

By order

Assistant Registrar,
ITAT, Bangalore.