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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

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Date of Decision: 21st July, 2015

\+ **ITA 416/2015**

COMMISSIONER OF INCOME TAX DELHI-21 ..... Appellant
Through: Ms. Suruchi Aggarwal, Senior Standing counsel with Ms. Lakshmi Gurung, Advocate.

versus

OM PRAKASH KHAITAN ..... Respondent

CORAM:
HON'BLE DR. JUSTICE S. MURALIDHAR
HON'BLE MR. JUSTICE VIBHU BAKHRU

Dr. S. MURALIDHAR, J.

CM No. 12085/2015 (for condonation of delay in re-filing the appeal)

1. For the reasons stated in the application, the delay in re-filing the appeal is condoned.

2. The application is disposed of.

ITA No. 416/2015

3. The challenge in this appeal under Section 260-A of the Income Tax Act, 1961 ('Act') is to an order dated 30th May 2014 passed by the Income Tax

Appellate Tribunal ('ITAT') in ITA No. 360/Del/2013 for the Assessment Year ('AY') 2009-10.

4. The Assessee is proprietor of M/s. O.P. Khaitan and Company, a firm of Solicitors and Advocates. The Assessee follows the cash system of accounting since inception and this has been consistently accepted by the Department since 1990. The Assessee receives advances from its clients for various legal matters for meeting out of pocket payments towards expenses in travelling, preparation of cases, engaging lawyers, etc. Such advance receipts are kept in a separate ledger account in the name of the client where all the expenses are debited from time to time. At the end of the year, credit balances in the accounts, where the matters were complicated or settled, are transferred to the Profit & Loss Account. Where the cases are pending, the credit balances are carried forward to the next year as sundry creditors.

5. For the year under consideration, the Assessing Officer ('AO') made an addition of Rs.10,78,01,478 representing balances outstanding on 31st October 2011 out of the total credit balance of Rs.20,79,97,695 as on 31st March 2009. The AO held that since the Assessee adopted the cash system of accounting, the taxing of the income could not be deferred to the subsequent years. Income had to be taxed in the year in which it was

received. Since the above amount had not been returned or shown as professional fee, it had to be taxed during the current AY. Further, as regards the amount earned from the investments made by the Assessee in mutual funds and shares, the AO concluded that there was a "direct and proximate nexus between the exempted income and the expenditures directly or indirectly involved in earning the said income" and therefore by invoking Section 14 A of the Act read with Rule 8D of the Income Tax Rules ('Rules') he worked out a disallowance of Rs. 8, 92,738.

6. The Assessee's appeal was allowed by the Commissioner of Income Tax (Appeals) [CIT (A)] and the above addition of Rs.10,78,01,478 was deleted. As regards the disallowance under Section 14 A of the Act read with Rule 8D of the Rules, the CIT (A) restricted it to Rs. 94,721 on the ground that no direct or indirect expenses were incurred for earning the exempt income.

7. In the consequent appeal by the Department, the ITAT noticed *inter alia* that the addition for the AY under consideration was similar to the ones made by the AO for AYs 2001-02 and 2003-04 and which had been deleted by the CIT (A) and concurred with by the ITAT. Nothing had been brought on record to persuade the ITAT to differ from the view taken by the ITAT in the Assessee's own case for those years. The ITAT also followed its

earlier order dated 3rd February 2006 in ITA No.1765/Del/2002 (*Jitender Sharma v. DCI*)' and order dated 25th August 2006 in ITA No.3820/Del/2004 (*M/s. Anand & Anand*). The ITAT acknowledged that although *res judicata* was not applicable to income tax proceedings "the principle of consistency requires that unless facts or law have/has undergone a change, the view taken earlier under similar circumstances needs must be followed."

8. Learned counsel for the Department has not questioned the above exposition of the law. The only ground urged before the Court is that the monies were kept invested by the Assessee in the mutual funds in the name of the Assessee and, therefore, had to be treated as income in his hands. However, as noted by the ITAT these facts were not new to the AY in question. The issue was whether the Assessee was consistently following a certain system of accounting which had been accepted by the Department. There is no change of system of accounting followed by the Assessee. Allowing the Department to adopt a different stance in the AY in question would create an anomalous situation as far as the Assessee is concerned. The issue of lawyers accepting monies from clients on account to defray the expenses and appropriating fees as income only upon completion of a case

has been examined in the past and a consistent view has been taken by the ITAT. This has been adverted to in the impugned order of the ITAT. The principles on the basis of which those decisions were taken are unexceptionable. Given the manner and functioning of the lawyers and law firms, it is correct that the categorisation of a receipt can take place only at the time of appropriation i.e. in case of fees only when the matter is over or as when the Assessee decides on the quantum of fees. This will not be the entire advance received as at the time it is received it does not bear any particular characterisation for the purposes of treating it as income.

9. As regards the second issue concerning the disallowance under Section 14A of the Act, the ITAT noticed the decision of its co-ordinate Bench in *Justice Sam P. Bharucha v. Addl, Commissioner of Income Tax, Mumbai 25 Taxmann.com 381 (Mum)*and observed that in the present case, the AO had not recorded any finding that any expenditure incurred by the Assessee was attributable for earning the exempt income. In order to disallow the expenditure there must be a nexus between the expenditure incurred and the income not forming part of the total income. Consequently, the disallowance under Section 14A of the Act was rightly deleted by the CIT (A) and affirmed by the ITAT.

10. The Court finds that no substantial question of law arises for determination by the Court from the impugned order of the ITAT.

11. The appeal is dismissed.

S. MURALIDHAR, J

VIBHU BAKHRU, J

JULY 21, 2015/dn