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THE
INCOME TAX REPORTS
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[2020] 425 ITR 1 (SC)

[In the Supreme Court of India]

UNION OF INDIA AND OTHERS
v.
EXIDE INDUSTRIES LIMITED AND ANOTHER

A. M. Khanwilkar, Hemant Gupta and Dinesh Maheshwari JJ.

April 24, 2020.

SS ▸ ITA 1961, s 43B(f) ; Constn of India, art 14, Part III
HF ▸ Department

Business expenditure—Deduction only on actual payment—Change of law—Amendment bringing liability to pay leave encashment to employees under provision—Valid—Liberty to assessee to follow mercantile system of accounting—Does not mean deduction against accrued liability cannot be regulated by law prospectively—Provision does not reverse nature of liability nor take away deduction—No limitation upon Legislature to include only particular type of deductions in section 43B—Other deductions specified in section also present and accrued liabilities—Court declaring liability to leave encashment an accrued liability—Contention that clause (f) enacted to defeat judgment of court not tenable—Income-tax Act, 1961, s. 43B(f).

Legislative powers—Parliament—Validity of provision—Presumption of validity—Objects and reasons—Non-disclosure—Does not render provision invalid.

Interpretation of taxing statutes—Validity of provisions—No ambiguity about legislative competence and import of enactment—Objects and reasons—No impact upon validity of provision unless provision ambiguous and possible interpretation violates Part III of Constitution—Unconscionability or

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ARBITRARINESS MUST BE SHOWN TO EXIST IN FORM, SUBSTANCE OR FUNCTIONING OF PROVISION—CONSTITUTION OF INDIA, PART III.

LEGISLATIVE POWERS—PARLIAMENT—DISCRIMINATION—TAXING STATUTES—LEGISLATURE HAS LARGER DISCRETION—CONSTITUTION OF INDIA, art. 14.

LEGISLATIVE POWERS—PARLIAMENT—ENACTMENT INVALIDATED BY COURT—LEGISLATURE FREE TO DIAGNOSE LAW AND ALTER INVALID ELEMENTS—DOES NOT MEAN LEGISLATURE DECLARES OPINION OF COURT INVALID.

Clause (f) of section 43B of the Income-tax Act, 1961, which makes the actual payment of liability to the employees in respect of leave encashment a condition precedent for extending the benefit of deduction under the Act, is valid.

In testing the Constitutional validity of a provision the fundamental concern of the court is to inspect the existence of enacting power and once such power is found to be present, the next examination is to ascertain whether the enacted provision impinges upon any right enshrined in Part III of the Constitution of India.

Whether a provision contravenes any right enshrined in Part III of the Constitution, either in its form, substance or effect begins with a presumption in favour of constitutionality because the power to legislate is the exclusive domain of the Legislature or Parliament. This power is clothed with power to decide when to legislate, what to legislate and how much to legislate. Thus, to decide the timing, content and extent of legislation is a function primarily entrusted to the Legislature and in exercise of judicial review, the court starts with a basic presumption in favour of the proper exercise of such power.

The objects and reasons behind the enactment of a statute signify the intention of the Legislature behind the enactment of a statutory provision. The purpose or underlying aim of a law can be discerned when interpreted in the light of stated objects and reasons. However, when there is no ambiguity about the legislative competence and of the import of the enactment, there is no rule, authority or convention to support the view that publication of the objects and reasons is quintessential for the sustenance of a duly enacted provision. In fact, objects and reasons are external aids to interpretation and can be looked into for the limited purpose in the process of interpretation.

When the court examines the validity of a provision, its primary concern is the literal text of the provision. This constitutes the first test of interpretation, often termed as the literal interpretation. If the text of the provision is

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unambiguous, the legislative intent gets coalesced and is epitomised therefrom. The court is not bound by such external elements. Therefore, the presence or absence of objects and reasons has no impact upon the constitutional validity of a provision as long as the literal features of the provision enable the court to comprehend its true meaning with sufficient clarity. The non-disclosure of objects and reasons per se would not impinge upon the constitutionality of a provision unless the provision is ambiguous and the possible interpretation violates Part III of the Constitution.

STATE OF WEST BENGAL *v.* UNION OF INDIA [1963] AIR 1963 SC 1241 *and* SANJEEV COKE MANUFACTURING COMPANY *v.* BHARAT COKING COAL LTD. [1983] 1 SCC 147 *relied on.*

The process of testing the validity is not to look into the prudence or proprieties of the Legislature in enacting the provision. Nor is it to examine the culpable conduct of the Legislature as an appellate authority over the Legislature. In the absence of any finding of any constitutional infirmity in a provision, the court is not empowered to invalidate a provision. To hold a provision violative of the Constitution on account of failure of the Legislature to state the objects and reasons would amount to an indirect scrutiny of the motives of the Legislature behind the enactment. Such a course of action is unwarranted. The time-tested principle of checks and balances does not empower the court to question the motives or wisdom of the Legislature, except in circumstances when they are demonstrated from the enacted law.

UNITED STATES *v.* BUTLER ET AL [1936] 297 US 1 *and* K. C. GAJAPATI NARAYAN DEO *v.* STATE OF ORISSA [1954] SCR 1 *relied on.*

Merely holding an enacted provision unconscionable or arbitrary is not sufficient to hold it unconstitutional unless such infirmities are sufficiently shown to exist in the form, substance or functioning of the provision.

The Legislature is the best forum to weigh different problems in the fiscal domain and form policies to address them including to create a new liability, exempt an existing liability, create a deduction or subject an existing deduction to new regulatory measures. In the very nature of taxing statutes, the Legislature holds the power to frame laws to plug in specific leakages. Such laws are only meant to target a specific avenue of taxability depending upon the experiences of tax evasion and tax avoidance at the ground level. The general principles of exclusion and inclusion do not apply to taxing statutes with the same vigour unless the law reeks of constitutional infirmities. While fiscal statutes must comply with the tenets of article 14, a larger discretion is given to the Legislature in taxing statutes than in other spheres.

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ANANT MILLS CO. LTD. *v.* STATE OF GUJARAT [1975] 2 SCC 175 *relied on.*

The Legislature cannot so to speak overrule a judgment of the Supreme Court. There cannot be any declaration of invalidating a judgment of the court without altering the legal basis of the judgment as a judgment is delivered with strict regard to the enactment as applicable at the relevant time. However, once the enactment itself stands corrected, the basic cause of adjudication stands altered and necessary effect follows. Upon an enactment being invalidated by the court, the Legislature is free to diagnose such law and alter the invalid elements thereof. In doing so, the Legislature does not declare the opinion of the court to be invalid.

INDIAN ALUMINIUM CO. *v.* STATE OF KERALA [1996] 7 SCC 637, WELFARE ASSOCIATION A. R. P., MAHARASHTRA *v.* RANJIT P. GOHIL [2003] 9 SCC 358 *and* STATE OF T. N. *v.* AROORAN SUGARS LTD. [1997] 1 SCC 326 *relied on.*

Clause (f) was inserted in section 43B by the Finance Act, 2001 with effect from April 1, 2002, in order to provide for a tax disincentive in cases of deductions claimed by the assessee from income-tax in lieu of liability accrued under the leave encashment scheme but not actually discharged by the employer. With the application of clause (f), the eligibility for deduction arises in the previous year in which the payment is actually made and not that in which provision was made in that regard, irrespective of the system of accounting followed by the assessee.

Generally, the heads of income to be subjected to taxability under the 1961 Act are enumerated in section 14 which starts with a saving clause and expressly predicates that profits and gains of business or profession shall be chargeable to income-tax. This general declaration of chargeability is followed by section 145, sub-section (1) of which prescribes the method of accounting and explicitly provides that the method of accounting is a prerogative falling in the domain of the assessee and an assessee is well within its rights to follow the mercantile system of accounting. Under the mercantile system of accounting, the assessment of income is made on the basis of accrual of liability and not on the basis of actual expenditure in lieu thereof. The expression "either cash or mercantile system of accounting" offers guidance on the nature of this accounting system. The right flowing from sub-section (1) is subject to the provisions of sub-section (2), which unambiguously empowers the Central Government to prescribe income computation and disclosure standards for accounting. Sub-section (2) is an enabling provision. It signifies that the general principle of autonomy of the assessee in adopting a

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system of accounting, is controlled by the regulation notified by the Central Government and must be adhered to by the class of assessee governed thereunder. There was a general dispensation of autonomy of the assessee to follow cash or mercantile system of accounting and the sole operative provision was section 145(1) of the 1961 Act that allowed complete autonomy to the assessee to follow the mercantile system. A limited change was brought about by the insertion of clause (f) in section 43B and nothing more. It applies prospectively. Merely because a liability has been held to be a present liability qualifying for instant deduction in terms of the applicable provisions at the relevant time that does not ipso facto mean that the deduction against such liability cannot be regulated by a law made by Parliament prospectively. It is open to the Legislature to withdraw statutory deductions prospectively. Clause (f) in section 43B inserted with prospective effect does not reverse the nature of the liability nor take away the deduction as such. The liability of leave encashment continues to be a present liability under the mercantile system of accounting and the insertion of clause (f) has not extinguished the autonomy of the assessee to follow the mercantile system. It merely defers the benefit of deduction to be availed of by the assessee for the purpose of computing his taxable income and links it to the date of actual payment thereof to the employee concerned. Thus, the only effect of the insertion of clause (f) is to regulate the deduction by putting it in a special provision.

Section 43B is enacted to provide for deductions to be availed of by the assessee in lieu of liabilities accruing in a previous year without making actual payment to discharge them. It does not place any embargo upon the autonomy of the assessee in adopting a particular method of accounting, nor deprive the assessee of any lawful deduction. It merely operates as an additional condition for the availment of deduction qua the specified head.

Section 43B opens with a non obstante clause. A non obstante clause assumes an overriding character against any other provision of general application. Out of the allowable deductions, the Legislature consciously earmarked certain deductions from time to time and included them in the ambit of section 43B so as to subject such deductions to the conditionality of actual payment. Such conditionality may have the inevitable effect of being different from the theme of the mercantile system of accounting on accrual of liability basis qua the specific head of deduction covered therein and not to other heads. But that is a matter for the Legislature and its wisdom in doing so.

Section 43B initially included deductions in respect of sum payable by the assessee by way of tax or duty or any sum payable by the employer by way of contribution to any provident fund or superannuation fund. The Legislature

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inserted more deductions to section 43B including cess, bonus or commission payable by employer, interest on loans payable to financial institutions and scheduled banks, payment in lieu of leave encashment by the employer and repayment of dues to the railways. There is no oneness or uniformity in the nature of deductions included in section 43B. It cannot be said that this section only provides for deductions concerning statutory liabilities. It is not unusual or abnormal for the Legislature to create a new liability, exempt an existing liability, create a deduction or subject an existing deduction to override regulations or conditions. In the basic scheme of section 43B, there is no direct or indirect limitation upon the power of Legislature to include only particular type of deductions in the ambit of section 43B. An external examination of this journey of section 43B reveals that the Legislature never restricted it to a particular category of deduction and that intent cannot be read into the main section by the court, while sitting in judicial review. The broad objective of enacting section 43B concerning specified deductions referred to therein was to protect larger public interest primarily of revenue including welfare of the employees. Clause (f) fits into that scheme and shares sufficient nexus with the broad objective.

The leave encashment scheme envisages the payment of a certain amount to employees in lieu of their unused paid leaves in a year. The nature of this payment is beneficial and pro-employee. It is not in the form of a bounty and forms a part of the conditions of service of the employee. An employer seeking deduction from tax liability in advance, in the name of discharging the liability of leave encashment, without actually extending such payment to the employee as and when the time for payment arises, may lead to abhorrent consequences. When the time for such payment arises, an employer may simply refuse to pay. The employee would be entangled in litigation claiming a hard-earned right and a double benefit would accrue to the employer. It is this mischief that clause (f) seeks to subjugate. The interpretation of a statute cannot be unrelated to the nature of the statute. In line with other clauses under section 43B, clause (f) was enacted to remedy a particular mischief and the concerns of public good, employees' welfare and prevention of fraud upon the Revenue are writ large in the clause. Such statutes are to be viewed through the prism of the mischief they seek to suppress.

HEYDON'S case [1584] 3 Co Rep 7 *and* STATE OF TAMIL NADU *v.* M.K. KANDASWAMI [1975] 36 STC 191 (SC) *applied.*

Clause (f) is in sync with other deductions specified in section 43B, which are also present and accrued liabilities. Irrespective of the category of liability, such deductions were regulated by law under the aegis of section 43B, keeping

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in mind the peculiar exigencies of fiscal affairs and underlying concerns of public revenue. A priori, merely because a certain liability has been declared to be a present liability by the court, it does not follow that the Legislature is denuded of its power to correct the mischief with prospective effect, including to create a new liability, exempt an existing liability, create a deduction or subject an existing deduction to new regulatory measures. Strictly speaking, the court cannot venture into hypothetical spheres while adjudging the constitutionality of a duly enacted provision and unfounded limitations cannot be read into the process of judicial review. A priori, the plea that clause (f) has been enacted with the sole purpose to defeat the judgment of the Supreme Court is misconceived.

Decision of the Calcutta High Court in EXIDE INDUSTRIES LTD. *v.* UNION OF INDIA [2007] 292 ITR 470 (Cal) *reversed.*

Cases referred to :

Anant Mills Co. Ltd. *v.* State of Gujarat [1975] 2 SCC 175 (para 34)
Bhanumati *v.* State of Uttar Pradesh [2010] 12 SCC 1 (para 11)
Bharat Earth Movers *v.* CIT [2000] 245 ITR 428 (SC) (para 4)
Exide Industries Ltd. *v.* Union of India [2007] 292 ITR 470 (Cal) (para 1)
Gajapati Narayan Deo (K. C.) *v.* State of Orissa [1954] SCR 1 (para 30)
Hari Singh *v.* The Military Estate Officer [1973] 1 SCR 515 (para 38)
Heydon's case [1584] 3 Co Rep 7 (para 21)
Indian Aluminium Co. *v.* State of Kerala [1996] 7 SCC 637 (para 38)
Kavalappara Kottarathil Kochuni *v.* States of Madras and Kerala [1960] AIR 1960 SC 1080 (para 24)
Kuldip Nayar *v.* Union of India [2006] 7 SCC 1 (para 11)
Manjula Bhashini (A.) *v.* Managing Director, A. P. Women's Co-operative Finance Corporation Ltd. [2009] 8 SCC 431 (para 24)
Sanjeev Coke Manufacturing Company *v.* Bharat Coking Coal Ltd. [1983] 1 SCC 147 (para 25)
State of Andhra Pradesh *v.* McDowell and Co. [1996] 3 SCC 709 (para 11)
State of Madhya Pradesh *v.* Rakesh Kohli [2012] 6 SCC 312 (para 11)
State of T. N. *v.* Arooran Sugars Ltd. [1997] 1 SCC 326 (para 38)
State of Tamil Nadu *v.* K. Shyam Sunder [2011] 8 SCC 737 (para 24)
State of Tamil Nadu *v.* M. K. Kandaswami [1975] 36 STC 191 (SC) (para 22)
State of West Bengal *v.* Union of India [1963] AIR 1963 SC 1241 (para 25)

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Tata Power Co. Ltd. *v.* Reliance Energy Ltd. [2009] 16 SCC 659 (para 24)

United States *v.* Butler et al [1936] 297 US 1 (para 30)

Welfare Association A. R. P., Maharashtra *v.* Ranjit P. Gohil [2003] 9 SCC 358 (para 38)

Civil Appeal No. 3545 of 2009.

Appeal from the judgment and order dated June 27, 2007 of the Calcutta High Court in A. P. O. No. 301 of 2005. The judgment of the High Court is reported as *Exide Industries Ltd.* v. *Union of India* [2007] 292 ITR 470 (Cal).

K. K. Venugopal, Attorney General, *Tushar Mehta* and *Ms. Madhavi Divan*, Additional Solicitors General (*Ms. Chinmayee Chandra, Ms. Nidhi Khanna* and *Mrs. Anil Katiyar*, Advocates, with them) for the appellants.

Dr. Aman Hingorani, Basu, Himanshu Yadav and *M/s. Hingorani and Associates,* Advocates, for the respondents.

JUDGMENT

The judgment of the court was delivered by

1 A. M. KHANWILKAR J.—In this appeal, the constitutional validity of clause (f) of section 43B of the Income-tax Act, 1961[1] arises for our consideration as a result of the decision of the High Court at Calcutta[2] vide order dated June 27, 2007 in A. P. O. No. 301 of 2005[3], wherein it is held that the said clause is arbitrary and violative of article 14 of the Constitution of India on various counts, as discussed hereinafter.

2 The stated clause (f) was inserted in the already existing section 43B vide Finance Act, 2001 with effect from April 1, 2002, in order to provide for a tax disincentive in cases of deductions claimed by the assessee from income tax in lieu of liability accrued under the leave encashment scheme but not actually discharged by the employer. This clause made the actual payment of liability to the employees as a condition precedent for extending the benefit of deduction under the 1961 Act. With the application of clause (f), the eligibility for deduction arises in the previous year in which the abovesaid payment is actually made and not in which provision was made in that regard, irrespective of the system of accounting followed by the assessee. Before we delve into further examination, we deem it appo-

1. For short, "the 1961 Act".
2. For short, "the High Court".
3. *Exide Industries Ltd*. v. *Union of India* [2007] 292 ITR 470 (Cal).

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site to reproduce the amended section 43B of the 1961 Act as applicable to the present case, which reads thus :

"43B. *Certain deductions to be only on actual payment.*—Notwithstanding anything contained in any other provision of this Act, a deduction otherwise allowable under this Act in respect of—

(a) any sum payable by the assessee by way of tax, duty, cess or fee, by whatever name called, under any law for the time being in force, or

(b) any sum payable by the assessee as an employer by way of contribution to any provident fund or superannuation fund or gratuity fund or any other fund for the welfare of employees, or

(c) any sum referred to in clause (ii) of sub-section (1) of section 36, or

(d) any sum payable by the assessee as interest on any loan or borrowing from any public financial institution or a State financial corporation or a State industrial investment corporation, in accordance with the terms and conditions of the agreement governing such loan or borrowing, or

(e) any sum payable by the assessee as interest on any term loan from a scheduled bank in accordance with the terms and conditions of the agreement governing such loan, or

(f) any sum payable by the assessee as an employer in lieu of any leave at the credit of his employee,

shall be allowed (irrespective of the previous year in which the liability to pay such sum was incurred by the assessee according to the method of accounting regularly employed by him) only in computing the income referred to in section 28 of that previous year in which such sum is actually paid by him :

Provided that nothing contained in this section shall apply in relation to any sum referred to in clause (a) or clause (c) or clause (d) or clause (e) or clause (f) which is actually paid by the assessee on or before the due date applicable in his case for furnishing the return of income under sub-section (1) of section 139 in respect of the previous year in which the liability to pay such sum was incurred as aforesaid and the evidence of such payment is furnished by the assessee along with such return :

Provided further that no deduction shall, in respect of any sum referred to in clause (b), be allowed unless such sum has actually been paid in cash or by issue of a cheque or draft or by any other mode on

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or before the due date as defined in the *Explanation* below clause (va) of sub-section (1) of section 36, and where such payment has been made otherwise than in cash, the sum has been realised within fifteen days from the due date.

Explanation 1.—For the removal of doubts, it is hereby declared that where a deduction in respect of any sum referred to in clause (a) or clause (b) of this section is allowed in computing the income referred to in section 28 of the previous year (being a previous year relevant to the assessment year commencing on the 1st day of April, 1983, or any earlier assessment year) in which the liability to pay such sum was incurred by the assessee, the assessee shall not be entitled to any deduction under this section in respect of such sum in computing the income of the previous year in which the sum is actually paid by him.

Explanation 2.—For the purposes of clause (a), as in force at all material times, 'any sum payable' means a sum for which the assessee incurred liability in the previous year even though such sum might not have been payable within that year under the relevant law.

Explanation 3.—For the removal of doubts it is hereby declared that where a deduction in respect of any sum referred to in clause (c) or clause (d) of this section is allowed in computing the income referred to in section 28 of the previous year (being a previous year relevant to the assessment year commencing on the 1st day of April, 1988, or any earlier assessment year) in which the liability to pay such sum was incurred by the assessee, the assessee shall not be entitled to any deduction under this section in respect of such sum in computing the income of the previous year in which the sum is actually paid by him.

Explanation 3A.—For the removal of doubts, it is hereby declared that where a deduction in respect of any sum referred to in clause (e) of this section is allowed in computing the income referred to in section 28 of the previous year (being a previous year relevant to the assessment year commencing on the 1st day of April, 1996, or any earlier assessment year) in which the liability to pay such sum was incurred by the assessee, the assessee shall not be entitled to any deduction under this section in respect of such sum in computing the income of the previous year in which the sum is actually paid by him.

Explanation 3B.—For the removal of doubts, it is hereby declared that where a deduction in respect of any sum referred to in clause (f) of this section is allowed in computing the income, referred to in sec-

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tion 28, of the previous year (being a previous year relevant to the assessment year commencing on the 1st day of April, 2001, or any earlier assessment year) in which the liability to pay such sum was incurred by the assessee, the assessee shall not be entitled to any deduction under this section in respect of such sum in computing the income of the previous year in which the sum is actually paid by him.

Explanation 4.—For the purposes of this section,—

(a) 'public financial institutions' shall have the meaning assigned to it in section 4A of the Companies Act, 1956 (1 of 1956) ;

(aa) 'scheduled bank' shall have the meaning assigned to it in the *Explanation* to clause (iii) of sub-section (5) of section 11 ;

(b) 'State financial corporation' means a financial corporation established under section 3 or section 3A or an institution notified under section 46 of the State Financial Corporations Act, 1951 (63 of 1951) ;

(c) 'State industrial investment corporation' means a Government company within the meaning of section 617 of the Companies Act, 1956 (1 of 1956), engaged in the business of providing long-term finance for industrial projects and eligible for deduction under clause (viii) of sub-section (1) of section 36."

3 The respondents, being liable to pay income tax upon the profits and gains of their business, found themselves aggrieved with the inclusion of clause (f) in section 43B and contended that section 145 of the 1961 Act offers them the choice of method of accounting and accordingly, they computed their profits and gains of business in accordance with the mercantile system. As per the mercantile system, income and expenditure are determined on the basis of accrual or provision and not on the basis of actual receipt/payment. The respondents further contended that section 43B has been carved out as an exception to the afore-stated general rule of accrual for determination of liability, as it subjects deductions in lieu of certain kinds of liabilities to actual payment. According to the respondents, the exception under section 43B comes into operation only in a limited set of cases covering statutory liabilities like tax, duty, cess, etc., and other liabilities created for the welfare of the employees and therefore, the liability under the leave encashment scheme being a trading liability cannot be subjected to the exception under section 43B of the 1961 Act.

4 It is the case of the respondents that the judgment of this court in *Bharat Earth Movers* v. *CIT*[1] holds the field of law as far as the nature of the

1. [2000] 245 ITR 428 (SC) ; [2000] 6 SCC 645.

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liability of leave encashment is concerned. The said judgment, while dealing with the principles of accounting under section 37, conclusively holds that if a business liability has arisen definitely, deduction may be claimed against the same in the previous year in which such liability has accrued, even if it has not been finally discharged. The court further held that the liability in lieu of leave encashment scheme is a present and definite liability and not a contingent liability. As regards the nature of the leave encashment liability, the respondents urge that this liability is carved in the nature of a beneficial provision and leave can only be encashed by the employees in accordance with the terms and conditions of employment. It is further contended that since the due date for encashment of leave does not arise in the same accounting year in which provision is made, there is no question of subjecting the deductions against such liability upon actual payment.

5 Having stated that all the clauses under section 43B, barring clause (f), cover liabilities of a statutory nature and those driven by concerns of the employees' welfare, the respondents would urge that the liability covered by clause (f) is of a completely distinct nature and without specifying clear objects and reasons for the inclusion of this liability under section 43B, it cannot be slipped into the main section. Further, the nature of this liability is neither in sync with the objects and reasons of the original section nor with those of other clauses enacted from time to time in different assessment years.

6 The respondents also urge that the enactment of clause (f) was driven by the sole consideration of subjugating the legal position expounded by this court in *Bharat Earth Movers* (supra) without removing the basis thereof. Such enactment would fall foul of the scheme of the Constitution. It would be an inroad into the sphere reserved exclusively for the judiciary and thereby violate the essential principles of separation of powers.

7 The validity of clause (f) faced judicial scrutiny first before the single Judge of the High Court. The clause passed the constitutional muster of the court, which had observed thus :

> "Thus the position of law existing at the date of insertion of clause (f) did not oblige the employer to actually pay the leave encashment benefit either to his employee or to any fund or to any third party, though the liability was an accrued one. If the employer, of his own accord, maintained a fund, he maintained it for his own convenience, and not because of any legal obligation. But in view of the mercantile system of accounting followed he was justified in showing the accrued liability and claiming deduction. There was nothing to pre-

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vent him from enjoying the benefit of deduction and at the same time from controlling and using the amount for his own benefit, till he was compelled to give the benefit of the leave in question to the employee concerned. It is evident that the clause was inserted to curb the abuse of existing law and protect the interests of the employee."

Addressing the argument that the insertion of the said clause was solely intended to defeat the judgment of this court in *Bharat Earth Movers* (supra), the learned single judge stated thus :

". . . It is true that the action neutralized the effect of the apex court decision in *Bharat Earth Movers* case, but I do not agree that it has amounted to encroachment upon the powers of the judiciary. Once the existing legal position was explained by their Lordships, I think, it was quite natural for the Legislature to examine the situation and legislate according to the need. The binding decision of the highest court was not nullified in the process ; only the position of law was changed prospectively."

8 The decision of the learned single judge was appealed and came to be reversed by the Division Bench of the High Court. The Division Bench, while holding clause (f) as unconstitutional, observed thus[1] :

". . . While inserting clause (f) no special reasons were disclosed. His Lordship held that such disclosure was not mandatory. We do not have any reason for disagreement on such issue provided the subject amendment could be termed as in furtherance to widen the scope of original section on the identical objects and reasons as disclosed at the time of enacting the original provision. As we find, the original section was incorporated to plug in deductions claimed by not discharging statutory liabilities. We also find that provision was subsequently made to restrict deductions on account of unpaid loan to the financial institutions. Leave encashment is neither statutory liability nor a contingent liability. It was a provision to be made for the entitlement of an employee achieved in a particular financial year. An employee earns certain amount by not taking leave which he or she is otherwise entitled to in that particular year. Hence, the employer is obliged to make appropriate provision for the said amount. Once the employee retires he or she has to be paid such sum on cumulative basis which the employee earns throughout his or her service career unless he or she avails of the leave earned by him or her. That, in our view, could not have any nexus with the original enactment. An employer is entitled to deduction for the expenditure he incurs for

1. Page 476 of 292 ITR.

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running his business which includes payment of salary and other perquisites to his employees. Hence, it is a trading liability. As such he is otherwise entitled to have deduction of such amount by showing the same as a provisional expenditure in his accounts. The Legislature by way of amendment restricts such deduction in case of leave encashment unless it is actually paid in that particular financial year. *The Legislature is free to do so after they disclose reasons for that and such reasons are not inconsistent with the main object of the enactment*. We are deprived of such reasons for our perusal . . ." (emphasis[1] supplied)

It also held that the subject matter of clause (f) was inconsistent with the original section 43B and observed as follows[2] :

". . . . We also do not find such enactment consistent with the original provision being section 43B which was originally inserted to plug in evasion of statutory liability. The apex court considered the situation in the case of *Bharat Earth Movers* (supra) when clause (f) was not there. The apex court, considering all aspect as disclosed by us hereinbefore, rejected the contention of the Revenue and granted appropriate deduction to the concerned assessee. The Legislature to get rid of the decision of the apex court brought out the amendment which would otherwise nullify the judge made law. The apex court decisions are judge made law and are applicable to all under the Constitution."

It is noteworthy that the High Court did not question the existence of power of the Legislature to enact the subject clause, as can be discerned from the following observations[2] :

"We do not for a single moment, observe that the Legislature was not entitled to bring such amendment. They were within their power to bring such amendment. However, they must disclose reason which would be consistent with the provisions of the Constitution and the laws of the land and not for the sole object of nullifying the apex court decision."

9 We shall now examine clause (f) on the touchstone of the Constitution, to be followed by an analysis of the impugned judgment.

10 We have heard Ms. Chinmayee Chandra, learned counsel for the appellants and Dr. Aman Hingorani, learned counsel for the respondents.

1. Here printed in italics.
2. Page 477 of 292 ITR.

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Constitutional validity of clause (f)

11 The approach of the court in testing the constitutional validity of a provision is well settled and the fundamental concern of the court is to inspect the existence of enacting power and once such power is found to be present, the next examination is to ascertain whether the enacted provision impinges upon any right enshrined in Part III of the Constitution. Broadly speaking, the process of examining validity of a duly enacted provision, as envisaged under article 13 of the Constitution, is premised on these two steps. No doubt, the second test of infringement of Part III is a deeper test undertaken in the light of settled constitutional principles. In *State of Madhya Pradesh* v. *Rakesh Kohli*[1], this court observed thus :

> "17. This court has repeatedly stated that legislative enactment can be struck down by court only on two grounds, namely (i) *that the appropriate Legislature does not have competence to make the law, and (ii) that it does not take away or abridge any of the fundamental rights enumerated in Part III of the Constitution or any other constitutional provisions. . . .*" (emphasis[2] supplied)

The above exposition has been quoted by this court with approval in a catena of other cases including *Bhanumati* v. *State of Uttar Pradesh*[3], *State of Andhra Pradesh* v. *McDowell and Co.*[4] and *Kuldip Nayar* v. *Union of India*[5], to state a few.

12 In furtherance of the two-fold approach stated above, the court, in *Rakesh Kohli* (supra) also called for a prudent approach to the following principles while examining the validity of statutes on taxability :

> "32. While dealing with constitutional validity of a taxation law enacted by Parliament or State Legislature, the court must have regard to the following principles :
>
> (i) there is always presumption in favour of constitutionality of a law made by Parliament or a State Legislature,
>
> (ii) no enactment can be struck down by just saying that it is arbitrary or unreasonable or irrational *but some constitutional infirmity has to be found,*
>
> (iii) the court is not concerned with the wisdom or unwisdom, the justice or injustice of the law as Parliament and State Legislatures are supposed to be alive to the needs of the people whom they represent

1. [2012] 6 SCC 312.
2. Here printed in italics.
3. [2010] 12 SCC 1.
4. [1996] 3 SCC 709.
5. [2006] 7 SCC 1.

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and they are the best judge of the community by whose suffrage they come into existence,

(iv) hardship is not relevant in pronouncing on the constitutional validity of a fiscal statute or economic law, and

(v) in the field of taxation, the Legislature enjoys greater latitude for classification." (emphasis[1] supplied)

13 In the present case, the legislative power of Parliament to enact clause (f) in the light of article 245 is not doubted at all. That brings us to the next step of examination, i.e., whether the said clause contravenes any right enshrined in Part III of the Constitution, either in its form, substance or effect. It is no more res integra that the examination of the court begins with a presumption in favour of constitutionality. This presumption is not just borne out of judicial discipline and prudence, but also out of the basic scheme of the Constitution wherein the power to legislate is the exclusive domain of the Legislature/Parliament. This power is clothed with the power to decide when to legislate, what to legislate and how much to legislate. Thus, to decide the timing, content and extent of legislation is a function primarily entrusted to the Legislature and in exercise of judicial review, the court starts with a basic presumption in favour of the proper exercise of such power.

14 Generally, the heads of income to be subjected to taxability under the 1961 Act are enumerated in section 14 which starts with a saving clause and expressly predicates that profits and gains of business or profession shall be chargeable to income tax. This general declaration of chargeability is followed by section 145, which prescribes the method of accounting and reads thus :

"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 assessees 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

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followed by the assessee, the Assessing Officer may make an assessment in the manner provided in section 144." (emphasis[1] supplied)

15 Sub-section (1) of section 145 explicitly provides that the method of accounting is a prerogative falling in the domain of the assessee and an assessee is well within its rights to follow the mercantile system of accounting. Be it noted that as per the mercantile system of accounting, the assessment of income is made on the basis of accrual of liability and not on the basis of actual expenditure in lieu thereof. The expression "either cash or mercantile system of accounting" offers guidance on the nature of this accounting system. Be that as it may, it is noteworthy that the right flowing from sub-section (1) is "subject to the provisions of sub-section (2)", which unambiguously empowers the Central Government to prescribe income computation and disclosure standards for accounting. Concededly, sub-section (2) is an enabling provision. It signifies that the general principle of autonomy of the assessee in adopting a system of accounting, is controlled by the regulation notified by the Central Government and must be adhered to by the class of assessee governed thereunder.

16 Section 43B, however, is enacted to provide for deductions to be availed of by the assessee in lieu of liabilities accruing in previous year without making actual payment to discharge the same. It is not a provision to place any embargo upon the autonomy of the assessee in adopting a particular method of accounting, nor deprives the assessee of any lawful deduction. Instead, it merely operates as an additional condition for the availment of deduction qua the specified head.

17 Section 43B bears heading "Certain deductions to be only on actual payment". It opens with a non obstante clause. As per settled principles of interpretation, a non obstante clause assumes an overriding character against any other provision of general application. It declares that within the sphere allotted to it by Parliament, it shall not be controlled or overridden by any other provision unless specifically provided for. Out of the allowable deductions, the Legislature consciously earmarked certain deductions from time to time and included them in the ambit of section 43B so as to subject such deductions to conditionality of actual payment. Such conditionality may have the inevitable effect of being different from the theme of mercantile system of accounting on accrual of liability basis qua the specific head of deduction covered therein and not to other heads. But that is a matter for the Legislature and its wisdom in doing so.

18 The existence of section 43B traces back to 1983 when the Legislature conceptualised the idea of such a provision in the 1961 Act. Initially, the

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provision included deductions in respect of sum payable by assessee by way of tax or duty or any sum payable by the employer by way of contribution to any provident fund or superannuation fund. It is noteworthy that the Legislature explained the inclusion of these deductions by citing certain practices of evasion of statutory liabilities and other liabilities for the welfare of employees. The scope and effect of the newly inserted provision was explained in paragraph 60 of the Memorandum Explaining the Provisions of the Finance Bill, 1983 as under[1] :

> "60 . . . To curb this practice, it is proposed to provide that deduction for any sum payable by the assessee by way of tax or duty under any law for the time being in force (irrespective of whether such tax or duty is disputed or not) or any sum payable by the assessee as an employer by way of contribution to any provident fund, or superannuation fund or gratuity fund or any other fund for the welfare of employees shall be allowed only in computing the income of that previous year in which such sum is actually paid by him."

With the passage of time, the Legislature inserted more deductions to section 43B including cess, bonus or commission payable by the employer, interest on loans payable to financial institutions, scheduled banks etc., payment in lieu of leave encashment by the employer and repayment of dues to the railways. Thus understood, there is no oneness or uniformity in the nature of deductions included in section 43B. It holds no merit to urge that this section only provides for deductions concerning statutory liabilities. Section 43B is a mixed bag and new and dissimilar entries have been inserted therein from time to time to cater to different fiscal scenarios, which are best determined by the Government of the day. It is not unusual or abnormal for the Legislature to create a new liability, exempt an existing liability, create a deduction or subject an existing deduction to override regulations or conditions.

19 The leave encashment scheme envisages the payment of a certain amount to the employees in lieu of their unused paid leaves in a year. The nature of this payment is beneficial and pro-employee. However, it is not in the form of a bounty and forms a part of the conditions of service of the employee. An employer seeking deduction from tax liability in advance, in the name of discharging the liability of leave encashment, without actually extending such payment to the employee as and when the time for payment arises may lead to abhorrent consequences. When time for such payment arises upon retirement (or otherwise) of the employee, an employer may simply refuse to pay. Consequently, the innocent employee will be

1. [1983] 140 ITR (St.) 141.

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entangled in litigation in the evening of his/her life for claiming a hard-earned right without any fault on his part. Concomitantly, it would entail in double benefit to the employer—advance deduction from tax liability without any burden of actual payment and refusal to pay as and when occasion arises. It is this mischief clause (f) seeks to subjugate.

20 The argument advanced by the respondents that the nature of leave encashment liability is such that it is impossible to make the actual payment in the same year, adds no weight to the claim of invalidity of the clause. We say so because the thrust of the provision is not to control the timing of payment, rather, it is strictly targeted to control the timing of claiming deduction in the name of such liability. The mischief sought to be remedied by this clause, as discussed above, clarifies the position.

21 Be it noted that the interpretation of a statute cannot be unrelated to the nature of the statute. In line with other clauses under section 43B, clause (f) was enacted to remedy a particular mischief and the concerns of public good, employees' welfare and prevention of fraud upon Revenue is writ large in the said clause. In our view, such statutes are to be viewed through the prism of the mischief they seek to suppress, that is, the *Heydon's* case[1] principle. In *Crawford, Statutory Construction*[2], it has been gainfully delineated that "an enactment designed to prevent fraud upon the Revenue is more properly a statute against fraud rather than a taxing statute, and hence should receive a liberal construction in the Government's favour.

22 In *State of Tamil Nadu* v. *M. K. Kandaswami*[3] this court expounded on the interpretation of remedial statutes thus[4] :

> "It may be remembered that section 7A is at once a charging as well as a remedial provision. Its main object is to plug leakage and prevent evasion of tax. *In interpreting such a provision, a construction which would defeat its purpose and, in effect, obliterate it from the statute book, should be eschewed.* If more than one construction is possible, that which preserves its workability, and efficacy is to be preferred to the one which would render it otiose or sterile. The view taken by the High Court is repugnant to this cardinal canon of interpretation." (emphasis[5] supplied)

23 Having ruled upon the constitutional validity of clause (f), we shall now examine the grounds on which the High Court ruled against its validity.

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1. [1584] 3 Co Rep 7.
2. CRAWFORD, Statutory Construction page 508.
3. [1975] 36 STC 191 (SC) ; [1975] 4 SCC 745.
4. Page 198 of 36 STC.
5. Here printed in italics.

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We may note that the respondents' challenge to the constitutional validity of the said clause has primarily been accepted on three grounds :

(i) Non-disclosure of objects and reasons behind its enactment and insertion into section 43B ;

(ii) Inconsistency of clause (f) with other clauses of section 43B and absence of nexus of the clause with the original enactment ;

(iii) Enactment has been triggered solely to nullify the dicta of this court in *Bharat Earth Movers* (supra).

Non-disclosure of objects and reasons

24 The objects and reasons behind the enactment of a statute signify the intention of the Legislature behind the enactment of a statutory provision. Indubitably, the purpose or underlying aim of a law can be discerned when interpreted in the light of stated objects and reasons. Inasmuch as, the settled canon of interpretation is to deduce the true intent of the Legislature, as the will of the people is constitutionally bestowed in the Legislature. It is true that an express objects and reasons would be useful in understanding the import of an enacted provision as and when the court is called upon to interpret the same. This court, in *State of Tamil Nadu* v. *K. Shyam Sunder*[1], laid emphasis upon the usefulness of objects and reasons in the process of interpretation and observed thus :

> "66. The Statement of Objects and Reasons appended to the Bill is not admissible as an aid to the construction of the Act to be passed, but it can be used for limited purpose of ascertaining the conditions which prevailed at that time which necessitated the making of the law, and the extent and urgency of the evil, which it sought to remedy. The Statement of Objects and Reasons may be relevant to find out what is the *objective* of any given statute passed by the Legislature. It may provide for the reasons which induced the Legislature to enact the statute. 'For the purpose of *deciphering the object and purport* of the Act, . . . the court can look to the Statement of Objects and Reasons thereof.' (emphasis[2] supplied) (Vide *Kavalappara Kottarathil Kochuni* v. *States of Madras and Kerala*, AIR 1960 SC 1080 and *Tata Power Co. Ltd.* v. *Reliance Energy Ltd.* [2009] 16 SCC 659, SCC page 686, para 79)
>
> 67. In *A. Manjula Bhashini* [2009] 8 SCC 431 this court held as under (SCC page 459, para 40) :

1. [2011] 8 SCC 737.
2. Here printed in italics.

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'40. The proposition which can be culled out from the aforementioned judgments is that although the Statement of Objects and Reasons contained in the Bill leading to enactment of the particular Act cannot be made the sole basis for construing the provisions contained therein, the same can be referred to for understanding the background, the antecedent state of affairs and the mischief sought to be remedied by the statute. The Statement of Objects and Reasons can also be looked into as an external aid for *appreciating the true intent of the Legislature* and/or the *object sought to be achieved* by enactment of the particular Act or for judging reasonableness of the classification made by such Act.' (emphasis[1] added)

68. Thus, in view of the above, the Statement of Objects and Reasons of any enactment spells out the core reason for which the enactment is brought and it can be looked into for appreciating the true intent of the Legislature or to find out the object sought to be achieved by enactment of the particular Act or even for judging the reasonableness of the classifications made by such Act."

Whereas, when there is no ambiguity about the legislative competence **25** and of the import of the enactment, no rule, authority or convention to support the view that publication of objects and reasons is quintessence for the sustenance of a duly enacted provision has been brought to our notice. In fact, objects and reasons feature in the list of external aids to interpretation and can be looked into for the limited purpose in the process of interpretation. Regard may be had to *State of West Bengal* v. *Union of India*[2], wherein the court expounded the legal position thus :

"13 . . . It is however well-settled that the Statement of Objects and Reasons accompanying a bill, when introduced in Parliament, cannot be used to determine the true meaning and effect of the substantive provisions of the statute. They cannot be used except for the limited purpose of understanding the background and the antecedent state of affairs leading up to the legislation. But we cannot use this statement as an aid to the construction of the enactment or to show that the Legislature did not intend to acquire the proprietary rights vested in the State or in any way to affect the State Governments' rights as owners of minerals. A statute, as passed by Parliament, is the expression of the collective intention of the Legislature as a whole, and any statement made by an individual, albeit a Minister, of the intention

1. Here printed in italics.
2. AIR 1963 SC 1241.

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> and objects of the Act cannot be used to cut down the generality of the words used in the statute."

The court was more categorical in restating the position in *Sanjeev Coke Manufacturing Company* v. *Bharat Coking Coal Ltd.*[1], where it noted :

> "25. No one may speak for Parliament and Parliament is never before the court. After Parliament has said what it intends to say, only the court may say what Parliament meant to say. None else. Once a statute leaves Parliament House, the court is the only authentic voice which may echo (interpret) the Parliament. This the court will do with reference to the language of the statute and other permissible aids . . ."

The express objects and reasons, therefore, serves a limited purpose of assisting the court in examining the validity of a provision, especially when the court is sitting over the interpretation of an ambiguous provision.

26 Indubitably, when the court examines the validity of a provision, its primary concern is the literal text of the provision. It is so because the Legislature speaks through the text and as long as it is not speaking in an equivocal manner, there is limited space for the court to venture beyond the text. This constitutes the first test of interpretation, often termed as the literal interpretation. If the text of the provision is unambiguous, the legislative intent gets coalesced and is epitomised therefrom.

27 In other words, when the textual element of the provision reeks of ambiguity and is susceptible to multiple meanings, the court enters into a proactive examination to find out the real meaning of the provision. This proactive examination by the court offers multiple avenues and methods to achieve the ultimate purpose of interpretation. Adverting to the express objects and reasons may be useful for limited purpose to understand the surrounding circumstances at the time of enactment. The court is not bound by such external elements, as discussed above. Therefore, the presence or absence of objects and reasons has no impact upon the constitutional validity of a provision as long as the literal features of the provision enable the court to comprehend its true meaning with sufficient clarity.

28 The Division Bench of the High Court, in the present case, plainly glossed over the fundamental presumption of constitutionality in favour of clause (f) and based its judgment upon the absence of objects and reasons as striking at the root of its validity. In our view, this approach is flawed for at least three reasons. Firstly, it steers clear from the necessary attempt to discover any constitutional infirmities in the enacted provision. Secondly, it

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1. [1983] 1 SCC 147

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makes no attempt to dissect the text of the provision so as to display the need to go beyond the text. Thirdly, it goes into the background of the enactment and ventures into a sphere which is out of bounds for the court as long as the need for interpretation borne out of any ambiguity arises.

29 The process of testing validity is not to sneak into the prudence or proprieties of the Legislature in enacting the impugned provision. Nor, is it to examine the culpable conduct of the Legislature as an appellate authority over the Legislature. The only examination of the court is restricted to the finding of a constitutional infirmity in the provision, as is placed before the court. Thus, the non-disclosure of objects and reasons per se would not impinge upon the constitutionality of a provision unless the provision is ambiguous and the possible interpretation violate Part III of the Constitution. In the absence of any finding of any constitutional infirmity in a provision, the court is not empowered to invalidate a provision.

30 To hold a provision as violative of the Constitution on account of failure of the Legislature to state the objects and reasons would amount to an indirect scrutiny of the motives of the Legislature behind the enactment. Such a course of action, in our view, is unwarranted. The raison d'etre behind this self-imposed restriction is because of the fundamental reason that different organs of the State do not scrutinise each other's wisdom in the exercise of their duties. In other words, the time-tested principle of checks and balances does not empower the court to question the motives or wisdom of the Legislature, except in circumstances when the same is demonstrated from the enacted law. The following instructive passage from *United States* v. *Butler et al*[1] offers guidance on the above proposition, wherein Justice Stone observed thus :

> "The power of courts to declare a statute unconstitutional is subject to two guiding principles of decision which ought never to be absent from judicial consciousness. One is that courts are concerned only with the power to enact statutes, not with their wisdom. The other is that while unconstitutional exercise of the power by the executive is subject to judicial restraint, the only check upon our own exercise of power by the executive is subject to judicial restraint. For the removal of unwise laws from the statute books appeal lies not to the courts but to the ballot and to the processes of democratic Government . . ."

In the Indian Constitutional jurisprudence, the above principle has been reckoned by this court in its early years in 1954 in *K. C. Gajapati Narayan Deo* v. *State of Orissa*[2], wherein the court observed thus :

1. [1936] 297 US 1.
2. [1954] SCR 1.

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". . . If the Legislature is competent to pass a particular law, the motives which impelled it to act are really irrelevant. On the other hand, if the Legislature lacks competency, the question of motive does not arise at all. Whether a statute is constitutional or not is thus always a question of power. If the Constitution of a State distributes the legislative powers amongst different bodies, which have to act within their respective spheres marked out by specific Legislature entries, or if there are limitations on the legislative authority in the shape of fundamental rights, questions do arise as to whether the Legislature in a particular case has or has not, in respect to the subject-matter of the statute or in the method of enacting it, transgressed the limits of its constitutional powers."

We have noted that the High Court has characterised clause (f) as "arbitrary" and "unconscionable" while imputing it with unconstitutionality. It is pertinent to note that the High Court reaches this conclusion without undertaking an actual examination of clause (f). Instead, the declaration is preceded by an enquiry into the circumstances leading up to the enactment. As discussed above, the constitutional power of judicial review contemplates a review of the provision, as it stands, and not a review of the circumstances in which the enactment was made. Be it noted that merely holding an enacted provision as unconscionable or arbitrary is not sufficient to hold it as unconstitutional unless such infirmities are sufficiently shown to exist in the form, substance or functioning of the impugned provision. No such infirmity has been exhibited and adverted to in the impugned judgment.

Inconsistency of clause (f) and absence of nexus with section 43B

31 The High Court has supported its finding of invalidity by recording two observations, vis-a-vis, the previously existing (unamended) clauses of section 43B - first, that clause (f) is inconsistent with other clauses and nature of deduction targeted in clause (f) is distinct from other deductions. Second, that clause (f) has no nexus with the objects and reasons behind the enactment of original section 43B and therefore, the objects and reasons attributed to section 43B cannot be used to deduce the object and purpose of clause (f).

32 At the outset, we observe that both the grounds are ill-founded. In the basic scheme of section 43B, there is no direct or indirect limitation upon the power of Legislature to include only particular type of deductions in the ambit of section 43B. To say that section 43B is restricted to deductions of a statutory nature would be nothing short of reading the provision in a purely imaginative manner. As already discussed above, from 1983

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onwards, section 43B had taken within its fold diverse nature of deductions, ranging from tax, duty to bonus, commission, railway fee, interest on loans and general provisions for welfare of employees. An external examination of this journey of section 43B reveals that the Legislature never restricted it to a particular category of deduction and that intent cannot be read into the main section by the court, while sitting in judicial review. Concededly, it is a provision to attach conditionality on deductions otherwise allowable under the Act in respect of specified heads, in that previous year in which the sum is actually paid irrespective of method of accounting.

33 Further, it be noted that the broad objective of enacting section 43B concerning specified deductions referred to therein was to protect larger public interest primarily of revenue including welfare of the employees. Clause (f) fits into that scheme and shares sufficient nexus with the broad objective, as already discussed hitherto.

34 Before stepping into the next ground, we are inclined to observe that the approach of constitutional courts ought to be different while dealing with fiscal statutes. It is trite that the Legislature is the best forum to weigh different problems in the fiscal domain and form policies to address the same including to create a new liability, exempt an existing liability, create a deduction or subject an existing deduction to new regulatory measures. In the very nature of taxing statutes, Legislature holds the power to frame laws to plug in specific leakages. Such laws are always pin-pointed in nature and are only meant to target a specific avenue of taxability depending upon the experiences of tax evasion and tax avoidance at the ground level. The general principles of exclusion and inclusion do not apply to taxing statutes with the same vigour unless the law reeks of constitutional infirmities. No doubt, fiscal statutes must comply with the tenets of article 14. However, a larger discretion is given to the Legislature in taxing statutes than in other spheres. In *Anant Mills Co. Ltd.* v. *State of Gujarat*[1], this court noted thus :

> "25 . . . But, in the application of the principles, the courts, in view of the inherent complexity of fiscal adjustment of diverse elements, permit a larger discretion to the Legislature in the matter of classification so long as it adheres to the fundamental principles underlying the said doctrine. The power of the Legislature to classify is of wide range and flexibility so that it can adjust its system of taxation in all proper and reasonable ways . . ."

Viewed thus, the reason weighed with the Division Bench of the High Court in the impugned judgment is untenable.

1. [1975] 2 SCC 175.

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Defeating the dictum in Bharat Earth Movers case

35 We shall now examine clause (f) on the ground that it defeats the judgment of this court in *Bharat Earth Movers* (supra). We have carefully analysed the decision in *Bharat Earth Movers* (supra) and note that the court was sitting in appeal over the nature of liability under the leave encashment scheme and held such liability to be a present liability. Resultantly, it became deductible from the profit and loss account of the assessee in the same accounting year in which provision against the same is made. The court rejected that leave encashment liability is a contingent one and observed thus[1] :

> "7. Applying the abovesaid settled principles to the facts of the case at hand we are satisfied that provision made by the appellant-company for meeting the liability incurred by it under the leave encashment scheme proportionate with the entitlement earned by employees of the company, inclusive of the officers and the staff, subject to the ceiling on accumulation as applicable on the relevant date, is entitled to deduction out of the gross receipts for the accounting year during which the provision is made for the liability. The liability is not a contingent liability. The High Court was not right in taking the view to the contrary."

36 Before the judgment in *Bharat Earth Movers* (supra), various Tribunals and High Courts across the country were treating the liability in lieu of leave encashment as a contingent liability. This did not go down well with the assessees following the mercantile accounting system, as they were not able to avail of deductions upon mere creation of a provision against such liability without making the actual payment. A challenge to this legal position reached before this court in *Bharat Earth Movers* (supra), wherein the court reversed the position.

37 It is no doubt true that the Legislature cannot sit over a judgment of this court or so to speak overrule it. There cannot be any declaration of invalidating a judgment of the court without altering the legal basis of the judgment — as a judgment is delivered with strict regard to the enactment as applicable at the relevant time. However, once the enactment itself stands corrected, the basic cause of adjudication stands altered and necessary effect follows the same. A legislative body is not supposed to be in possession of a heavenly wisdom so as to contemplate all possible exigencies of their enactment. As and when the Legislature decides to solve a problem, it has multiple solutions on the table. At this stage, Parliament exercises its legislative wisdom to shortlist the most desirable solution and

1. Page 432 of 245 ITR.

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enacts a law to that effect. It is in the nature of a "trial and error" exercise and we must note that a law-making body, particularly in statutes of fiscal nature, is duly empowered to undertake such an exercise as long as the concern of legislative competence does not come into doubt. Upon the law coming into force, it becomes operative in the public domain and opens itself to any review under Part III as and when it is found to be plagued with infirmities. Upon being invalidated by the court, the Legislature is free to diagnose such law and alter the invalid elements thereof. In doing so, the Legislature is not declaring the opinion of the court to be invalid.

38 In *Welfare Association A. R. P., Maharashtra* v. *Ranjit P. Gohil*[1], this court relied upon *Indian Aluminium Co.* v. *State of Kerala*[2] and upon elaborate analysis, laid down certain principles to preserve the delicate balance of separation of powers and observed thus :

> "47. . . . (v) in exercising legislative power, the Legislature by mere declaration, without anything more, cannot directly overrule, revise or override a judicial decision. It can render judicial decision ineffective by enacting valid law on the topic within its legislative field fundamentally altering or changing its character retrospectively. The changed or altered conditions are such that the previous decision would not have been rendered by the court, if those conditions had existed at the time of declaring the law as invalid. . . . It is competent for the Legislature to enact the law with retrospective effect ;
>
> (vi) the consistent thread that runs through all the decisions of this court is that the Legislature cannot directly overrule the decision or make a direction as not binding on it but has power to make the decision ineffective by removing the base on which the decision was rendered, consistent with the law of the Constitution and the Legislature must have competence to do the same."

The court then relied upon *State of T. N.* v. *Arooran Sugars Ltd.*[3] to reaffirm the point and noted thus :

> "48. In *State of Tamil Nadu* v. *Arooran Sugars Ltd.*, the Constitution Bench made an exhaustive review of all the available decisions on the point and summed up the law by holding :
>
> 'It is open to the Legislature to remove the defect pointed out by the court or to amend the definition or any other provision of the Act in question retrospectively. In this process it cannot be said that there has been an encroachment by the Legislature over the power of the

1. [2003] 9 SCC 358.
2. [1996] 7 SCC 637.
3. [1997] 1 SCC 326.

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judiciary. A court's directive must always bind unless the conditions on which it is based are so fundamentally altered that under altered circumstances such decisions could not have been given. This will include removal of the defect in a statute pointed out in the judgment in question, as well as alteration or substitution of provisions of the enactment on which such judgment is based, with retrospective effect'."

In *Indian Aluminium Co.* (supra), the court relied upon a set of authorities and extended its approval to the above stated position of law thus :

"41 . . . A Constitution Bench of this court had held that the distinction between legislative act and judicial act is well-known. The adjudication of the rights of the parties is a judicial function. The Legislature has to lay down the law prescribing the norms or conduct which will govern the parties and transactions to require the court to give effect to that law. Validating legislation which removes the norms of invalidity of action or providing remedy is not an encroachment on judicial power. Statutory rule made under the proviso to article 309 was upheld. *The Legislature cannot by a bare declaration without anything more, directly overrule, reverse or override a judicial decision at any time in exercise of the plenary power conferred on the Legislature by articles 245 and 246 of the Constitution. It can render a judicial decision ineffective by enacting a valid law on a topic within its legislative field, fundamentally altering or changing with retrospective, curative or nullifying effect, the conditions on which such a decision is based*. In *Hari Singh* v. *The Military Estate Officer* [1973] 1 SCR 515, prior to 1958 two alternative modes of eviction under Public Premises Act were available. When the eviction was sought of an unauthorised occupant by summary procedure the constitutionality thereof was challenged and upheld. The Act was subsequently amended in 1958 with retrospective operation from September 16, 1958. Thereunder only one procedure for eviction was available. It was contended to be a legislative encroachment of judicial power. A Bench of three judges held that the Legislature possessed competence over the subject matter and the Validation Act could remove the defect which the court had found in the previous case. It was not the legislative encroachment of judicial power but one of removing the defect which the court had pointed out with a deeming date." (emphasis[1] supplied)

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1. Here printed in italics.

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39 Reverting to the true effect of the reported judgment under consideration, it was rendered in the light of general dispensation of autonomy of the assessee to follow cash or mercantile system of accounting prevailing at the relevant time, in the absence of an express statutory provision to do so differently. It is an authority on the nature of the liability of leave encashment in terms of the earlier dispensation. In the absence of any such provision, the sole operative provision was section 145(1) of the 1961 Act that allowed complete autonomy to the assessee to follow the mercantile system. Now a limited change has been brought about by the insertion of clause (f) in section 43B and nothing more. It applies prospectively. Merely because a liability has been held to be a present liability qualifying for instant deduction in terms of the applicable provisions at the relevant time does not ipso facto signify that deduction against such liability cannot be regulated by a law made by Parliament prospectively. In the matter of statutory deductions, it is open to the Legislature to withdraw the same prospectively. In other words, once the Finance Act, 2001 was duly passed by Parliament inserting clause (f) in section 43B with prospective effect, the deduction against the liability of leave encashment stood regulated in the manner so prescribed. Be it noted that the amendment does not reverse the nature of the liability nor has it taken away the deduction as such. The liability of leave encashment continues to be a present liability as per the mercantile system of accounting. Further, the insertion of clause (f) has not extinguished the autonomy of the assessee to follow the mercantile system. It merely defers the benefit of deduction to be availed of by the assessee for the purpose of computing his taxable income and links it to the date of actual payment thereof to the employee concerned. Thus, the only effect of the insertion of clause (f) is to regulate the stated deduction by putting it in a special provision.

40 Notably, this regulatory measure is in sync with other deductions specified in section 43B, which are also present and accrued liabilities. To wit, the liability in lieu of tax, duty, cess, bonus, commission etc. also arise in the present as per the mercantile system, but assessees used to defer payment thereof despite claiming deductions thereagainst under the guise of mercantile system of accounting. Resultantly, irrespective of the category of liability, such deductions were regulated by law under the aegis of section 43B, keeping in mind the peculiar exigencies of fiscal affairs and underlying concerns of public revenue. A priori, merely because a certain liability has been declared to be a present liability by the court as per the prevailing enactment, it does not follow that Legislature is denuded of its power to correct the mischief with prospective effect, including to create a new

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liability, exempt an existing liability, create a deduction or subject an existing deduction to new regulatory measures. Strictly speaking, the court cannot venture into hypothetical spheres while adjudging constitutionality of a duly enacted provision and unfounded limitations cannot be read into the process of judicial review. A priori, the plea that clause (f) has been enacted with the sole purpose to defeat the judgment of this court is misconceived.

41 The position of law discussed above leaves no manner of doubt as regards the legitimacy of enacting clause (f). The respondents have neither made a case of non-existence of competence nor demonstrated any constitutional infirmity in clause (f).

42 In view of the clear legal position explicated above, this appeal deserves to be allowed. Accordingly, the impugned judgment of the Division Bench of the High Court is reversed and clause (f) in section 43B of the 1961 Act is held to be constitutionally valid and operative for all purposes. No order as to costs. Pending interlocutory applications, if any, shall stand disposed of.

[2020] 425 ITR 30 (SC)

[IN THE SUPREME COURT OF INDIA]

UNION OF INDIA AND ANOTHER

v.

U. A. E. EXCHANGE CENTRE

A. M. KHANWILKAR and AJAY RASTOGI JJ.

April 24, 2020.

SS 4 ITA 1961, ss 2(13), (24), 5(2), 9(1)(i) *Expln 2* ; DTAA (UAE), arts 5, 7
AY ▸ 2000-01 to 2003-04
HF ▸ Assessee

NON-RESIDENT—TAXABILITY IN INDIA—PERMANENT ESTABLISHMENT—ASSESSEE, A COMPANY INCORPORATED IN UNITED ARAB EMIRATES, OFFERING REMITTANCE SERVICES FOR TRANSFERRING FUNDS FROM UAE TO INDIA—FUNDS COLLECTED FROM NON-RESIDENT INDIAN REMITTER BY ASSESSEE IN UAE CHARGING ONE-TIME FEE—FUNDS REMITTED ON BEHALF OF NON-RESIDENT INDIAN CUSTOMER BY SENDING INSTRUMENTS OR CHEQUES THROUGH LIAISON OFFICES TO BENEFICIARIES IN INDIA—PARTICULARS OF REMITTANCES DOWNLOADED BY LIAISON OFFICE IN INDIA BY ACCESSING MAIN SERVERS OF ASSESSEE IN UAE—CHEQUES OR DRAFTS DRAWN ON BANKS IN INDIA PRINTED OUT AND COURIERED OR DISPATCHED TO BENEFICIARIES IN INDIA, IN ACCORDANCE WITH INSTRUCTIONS OF NON-RESIDENT INDIAN REMITTER—ACTIVITIES OF LIAISON

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OFFICES OF PREPARATORY OR AUXILIARY CHARACTER—TRANSACTIONS COMPLETED WITH REMITTERS IN UAE—NO PERMISSION GIVEN BY RESERVE BANK OF INDIA TO ASSESSEE TO ENGAGE IN PRIMARY BUSINESS ACTIVITY AND ESTABLISH A BUSINESS CONNECTION—LIAISON OFFICE IN INDIA WOULD NOT QUALIFY AS PERMANENT ESTABLISHMENT—NO INCOME EARNED BY LIAISON OFFICE IN INDIA—EVEN IF ACTIVITIES OF LIAISON OFFICE REGARDED AS BUSINESS ACTIVITY, THEY WERE "OF PREPARATORY OR AUXILIARY CHARACTER" AND NOT AMENABLE TO TAX LIABILITY—INCOME-TAX ACT, 1961, ss. 2(13), (24), 5(2), 9(1)(i), *Expln. 2*—DOUBLE TAXATION AVOIDANCE AGREEMENT BETWEEN INDIA AND UNITED ARAB EMIRATES, arts. 5, 7[1].

The assessee-company was incorporated in the United Arab Emirates and offered remittance services for transferring amounts from the UAE to various places in India. It obtained approval from the Reserve Bank of India for establishing liaison offices in India subject to certain conditions such as that the offices in India would not undertake any other activity of a trading, commercial or industrial nature except the work mentioned in the approval letter, nor enter into any business contracts in its own name without prior permission, and that the entire expenses of the office in India would be met exclusively out of the funds received from abroad through normal banking channels. The assessee set up liaison offices in Cochin, Chennai, New Delhi, Mumbai and Jalandhar in India. The entire expenses of the liaison offices in India were met exclusively out of funds received from the UAE through normal banking channels. The liaison offices undertook no activity of trading, commercial or industrial nature. No fee or commission was charged or received in India by any of the liaison offices for services rendered in India. The assessee collected the funds to be transferred from the non-resident Indian remitter by the assessee in the UAE charging a one-time fee, and thereafter made an electronic remittance of the funds on behalf of its non-resident Indian customer in two ways : by telegraphic transfer through bank channels, or on the request of the non-resident Indian remitter, by sending instruments or cheques through its liaison offices to the beneficiaries in India, designated by the non-resident Indian remitter. In the second mode of remittance, the liaison office in India downloaded the particulars of remittances through electronic media and printing cheques or drafts drawn on the banks in India, which, in turn, were couriered or dispatched to the beneficiaries in India, in accordance with the instructions of the non-resident Indian remitter. While doing this, the liaison office of the assessee remained connected with its main server in the

1. [1994] 205 ITR (St.) 49.

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UAE, as the information was contained in the main server thereat, which could be accessed by the liaison office in India for the purpose of remittance of funds to the beneficiaries in India by the non-resident Indian remitters. For the assessment years 1998-99 to 2003-04, the assessee filed returns showing nil income, on the basis that no income had accrued or was deemed to have accrued to it in India, either under the Income-tax Act, 1961 or the Double Taxation Avoidance Agreement between India and the United Arab Emirates. The returns were accepted by the Department. The assessee, however, entertaining some doubts, filed an application before the Authority for Advance Rulings seeking a ruling on the question whether any income accrued or was deemed to have accrued in India from the activities carried out by the company in India. The Authority answered the question in the affirmative, holding that income shall be deemed to accrue in India from the activity carried out by the liaison offices of the assessee in India as it had carried on business in India through a permanent establishment situated in India and the profits of the enterprise needed to be taxed in India, but only so much thereof as attributable to the liaison offices in India (see UAE Exchange Centre LLC, *In re* [2004] 268 ITR 9 (AAR)*). Following the ruling of the Authority, the Department issued four notices under section 148 of the Act for the assessment years 2000-01, 2001-02, 2002-03 and 2003-04. The assessee filed a writ petition upon which the High Court held (see* U. A. E. Exchange Centre Ltd. *v.* Union of India [2009] 313 ITR 94 (Delhi)*) that the nature of activities carried on by the assessee in the liaison offices being only of preparatory and auxiliary character, they were clearly excluded by virtue of the deeming provision, that the activity carried on by the liaison offices of the assessee in India did not in any manner contribute directly or indirectly to the earning of profits or gains by the assessee in the UAE, that every aspect of the transaction was concluded in the UAE, and the activity performed by the liaison offices in India was only supportive of the transaction carried on in the UAE. The High Court quashed the ruling of the Authority and the notices issued by the Department under section 148 but gave liberty to the Department to proceed against the assessee on any other ground, as permissible in law. On appeal :*

Held, *dismissing the appeal, (i) that although the assessee was engaged in "business" and had "business connections", for which, by virtue of the deeming provision and the sweep of sections 2(24), 4 and 5 read with section 9 of the Act, it would be a case of income deemed to accrue or arise in India to the assessee, in the present case, the matter in issue had to be answered on the basis of the stipulations in the Agreement notified in exercise of powers conferred under section 90 of the Act.*

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UNION OF INDIA *v.* AZADI BACHAO ANDOLAN [2003] 263 ITR 706 (SC) *applied.*

(ii) That the place from where the activities were carried on by the assessee in India was a liaison office and would, therefore, be covered by the term permanent establishment in article 5(2) of the Double Taxation Avoidance Agreement between India and the United Arab Emirates. However, article 5(3) of the Agreement opens with a non obstante clause and predicates that notwithstanding the preceding provisions of the article, which would mean paragraphs (1) and (2) of article 5, it would still not be a permanent establishment, if any of the clauses in article 5(3) are applicable. For that, the functional test regarding the activity in question would be essential. Assuming that the activities of the liaison offices of the assessee were business activities, since they were of preparatory or auxiliary character, they would fall within the excepted category under article 5(3)(e) of the Agreement. Resultantly, the liaison office could not be regarded as a permanent establishment within the sweep of article 7 of the Agreement. The crucial activities were of downloading particulars of remittances through electronic media and then printing cheques or drafts drawn on the banks in India, which, in turn, were couriered or dispatched to the beneficiaries in India, in accordance with the instructions of the non-resident Indian remitter. While doing so, the liaison offices of the assessee in India remained connected with its main server in the UAE and the information residing thereat was accessed by the liaison office in India for the purpose of remittance of funds to the beneficiaries in India by the non-resident Indian remitters. These were a combination of virtual and physical activities unlike the virtual activity of funds being remitted by telegraphic transfer through banking channels. The permission given by the Reserve Bank of India to the assessee was limited to the activities which the assessee had been permitted to carry on within India. This permission did not allow the assessee to enter into a contract with anyone in India, but only to provide service of delivery of cheques or drafts drawn on the banks in India. The assessee was not to render any consultancy or any other service, directly or indirectly, with or without any consideration nor borrow or lend any money from or to any person in India without prior permission of the Reserve Bank of India. The conditions made it amply clear that the office in India could not undertake any other activity of trading, commercial or industrial nature, nor enter into any business contracts in its own name without prior permission of the Reserve Bank of India. The liaison office of the assessee in India could not even charge commission or fee or receive any remuneration or income in respect of the activities undertaken by the liaison office in India. The activities

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carried on by the liaison office of the assessee in India as permitted by the Reserve Bank of India, clearly demonstrated that the assessee could not engage in any primary business activity and establish a business connection as such. It could carry on activities of preparatory or auxiliary nature only. The activities in question of the liaison offices of the assessee in India were circumscribed by the permission given by the Reserve Bank of India and were of preparatory or auxiliary character and, therefore, covered by article 5(3)(e). As a result, the fixed place used by the assessee as liaison office in India, would not qualify under the definition of permanent establishment in terms of article 5(1) and (2) of the Agreement on account of the non obstante and deeming clause in article 5(3) of the Agreement.

DIT (INTERNATIONAL TAXATION) *v.* MORGAN STANLEY AND CO. INC. [2007] 292 ITR 416 (SC) *applied.*

(iii) That thus, it followed that the assessee was not carrying on any business activity in India as such, but only dispensing the remittances by downloading information from the main server of the assessee in the UAE and printing cheques or drafts drawn on the banks in India in accordance with the instructions given by the non-resident Indian remitters in the UAE. The transactions had completed with the remitters in the UAE, and no charges towards fee or commission could be collected by the liaison office in India in that regard. To put it differently, no income as specified in section 2(24) of the Act was earned by the liaison office in India especially because the liaison office was not a permanent establishment in terms of article 5 of the Agreement (as it only carried on activity of a preparatory or auxiliary character). In that case, the deeming provisions in sections 5 and 9 of the Act could have no bearing whatsoever. No tax could be levied or collected from the liaison office of the assessee in India in respect of the primary business activities consummated by the assessee in the UAE.

(iv) That Explanation 2 *to section 9(1)(i) gives the meaning of the expressions "business connection" and "business activity". However, even if the activities of the liaison office of the assessee in India were regarded as business activity, they were "of preparatory or auxiliary character". By virtue of article 5(3)(e) of the Agreement, the fixed place of business (liaison office) of the assessee in India, otherwise a permanent establishment, was deemed to be expressly excluded from being so. And since by a legal fiction it was deemed not to be a permanent establishment of the assessee in India, it was not amenable to tax liability in terms of article 7 of the Agreement.*

Decision of the Delhi High Court in U. A. E. EXCHANGE CENTRE LTD. *v.* UNION OF INDIA [2009] 313 ITR 94 (Delhi) *affirmed.*

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Cases referred to :

Anglo-French Textile Co. Ltd. *v.* CIT [1953] 23 ITR 101 (SC) (para 4)

Arabian Express Line Ltd. of United Kingdom *v.* Union of India [1995] 212 ITR 31 (Guj) (para 8)

CIT *v.* Davy Ashmore India Ltd. [1991] 190 ITR 626 (Cal) (para 8)

CIT *v.* R. D. Aggarwal and Co. [1965] 56 ITR 20 (SC) (para 3)

CIT *v.* R. M. Muthaiah [1993] 202 ITR 508 (Karn) (para 8)

CIT *v.* Visakhapatnam Port Trust [1983] 144 ITR 146 (AP) (para 8)

DIT (Asst.) *v.* E-Funds IT Solution Inc. [2017] 399 ITR 34 (SC) (para 12)

DIT (International Taxation) *v.* Morgan Stanley and Co. Inc. [2007] 292 ITR 416 (SC) (paras 4, 10)

Leonhardt Andra und Partner, GmbH *v.* CIT [2001] 249 ITR 418 (Cal) (para 8)

U. A. E. Exchange Centre Ltd. *v.* Union of India [2009] 313 ITR 94 (Delhi) (para 4)

UAE Exchange Centre LLC, *In re* [2004] 268 ITR 9 (AAR) (para 3)

Union of India *v.* Azadi Bachao Andolan [2003] 263 ITR 706 (SC) (para 4)

Civil Appeal No. 9775 of 2011.

Appeal from the judgment and order dated February 13, 2009 of the Delhi High Court in W. P. (C) No. 14869 of 2004. The judgment of the High Court is reported as *U. A. E. Exchange Centre Ltd.* v. *Union of India* [2009] 313 ITR 94 (Delhi).

Arijit Prasad, Senior Advocate, (*Ms. Niranjana Singh, Ms. Purnima Bhat, Ms. Anil Katiyar* and *B. V. Balaram Das*, Advocates, with him) for the appellants.

H. P. Ranina, Vishnu B. Saharya, Viresh B. Saharya, Vivek B. Saharya, Akshat Agarwal and *M/s. Saharya and Co.,* Advocates, for the respondent.

JUDGMENT

The judgment of the court was delivered by

1 A. M. KHANWILKAR J.—The respondent is a limited company incorporated in the United Arab Emirates (UAE). It is engaged in offering, among others, remittance services for transferring amounts from UAE to various places in India. It had applied for a permission under section 29(1)(a) of the Foreign Exchange Regulation Act, 1973 (for short, "the 1973 Act"), pursuant to which approval was granted by the Reserve Bank of India (for

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short, "the RBI") vide letter dated September 24, 1996. The same reads thus :

"Telegrams "Reserve Bank" Bombay	Reserve Bank of India Exchange Control Department Central Office Building Bombay 400 023	Post Box No. 1055

Please quote Ref. in Reply

Ref. No. EC Co. FID(I)/137/10-I-05-02/3975 (Activity)/96-97

BY AIR MAIL/REGISTERED A.D.

U.A.E. Exchange Centre L.L.C.,

24 Sep 1996

Post Box 170,

Abu Dhabi,

UAE.

Dear Sirs,

Permission under section 29(1)(a) of the Foreign Exchange Regulation Act, 1973 for opening a liaison office in India.

Please refer to your application dated Nil and the correspondence resting with your letter Ref. UAEEC/HO/479/96 dated August 9, 1996 on the captioned subject.

2. We advise that we are agreeable to your establishing a liaison office at Cochin initially for a period of three years to enable you to (i) respond quickly and economically to enquiries from correspondent banks with regard to suspected fraudulent drafts, (ii) to undertake reconciliation of bank accounts held in India, (iii) to act as a communication centre receiving computer (via Modem) advices of mail transfer T.T. stop payments messages, payments details etc., originating from your several branches in UAE and transmitting to your Indian correspondent banks, (iv) Printing Indian Rupee drafts with facsimile signature from the Head Office and counter signature by the authorised signatory of the Office at Cochin, (v) following up with the Indian correspondent banks.

3. Please note that this permission has been granted subject to the following conditions :

(i) Except the above mentioned work, the office in India will not undertake any other activity of trading, commercial or industrial nature nor shall it enter into any business contracts in its own name without our prior permission.

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(ii) No commission/fees will be charged or any other remuneration received/income earned by the office in India for any activity undertaken by it as listed in para 2 of this letter or otherwise in India.

(iii) The entire expenses of the office in India will be met exclusively out of the funds received from abroad through normal banking channels.

(iv) The liaison office in India shall not borrow or lend any money from/to any person in India without our prior permission.

(v) The liaison office in India shall not acquire, hold (otherwise than by way of lease for a period not exceeding five years), transfer or dispose of any immovable property in India without obtaining prior permission of the Reserve Bank of India under section 31 of the Foreign Exchange Regulation Act, 1973.

(vi) The liaison office in India will furnish to our Cochin Regional Office (on a yearly basis) :

(a) a certificate from the auditors to the effect that during the year no income was earned by/or accrued to the office in India ;

(b) details of remittances received from abroad duly supported by Inward Remittance Certificates ;

(c) certified copy of the audited final accounts of the office in India ; and

(d) annual report of the work done by the office in India, stating therein the details of actual remittances received from NRI through your office during the period in respect of which the office had rendered liaison services.

(e) The number of staff engaged/appointed and duties assigned to each staff.

(vii) The incharge of the liaison office in India will not have signing/commitment powers except than those which are required for normal functioning of liaison office on behalf of the Head Office.

(viii) The liaison office will not render any consultancy or any other services directly/indirectly, with or without any consideration.

4. In case you desire to open a head office account in the books of your liaison office in India, we hereby grant you our approval to maintain such an account subject to the conditions that the credits to the account should represent the funds received from head office through normal banking channels for meeting the expenses of the office and no other amount should be credited without prior permission of the Reserve Bank of India. Similarly debits to this account

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could be raised only for meeting the local expenses of the office. Audited transcript of the head office account may be forwarded to our Cochin Regional Office along with the annual accounts mentioned above.

5. It is further clarified that the permission granted hereby is limited to and for the purpose of the provisions of section 29 ibid only and shall not be construed in any way as regularising, condoning or in any manner validating any irregularities, contraventions or other lapses if any under the provisions of any other law for the time being in force.

6. Please note to furnish to us the postal address of your liaison office in due course for our record. You may also note to address the correspondence in future to our Cochin Regional Office.

7. Please acknowledge receipt.

Yours faithfully,

(Sd.) . . . .
Prashant Saran
Deputy General Manager."

2 The respondent set up its first liaison office in Cochin, Kerala (India) in January, 1997 and thereafter, in Chennai, New Delhi, Mumbai and Jalandhar in India. The activities carried on by the respondent from the said liaison offices are stated to be in conformity with the terms and conditions prescribed by the RBI in its letter dated September 24, 1996. The entire expenses of the liaison offices in India are met exclusively out of funds received from UAE through normal banking channels. Indisputably, it is asserted by the respondent that its liaison offices undertake no activity of trading, commercial or industrial, as the case may be. The respondent has no immovable property in India otherwise than by way of lease for operating the liaison offices. No fee/commission is charged or received in India by any of the liaison offices for services rendered in India. It is claimed that no income accrues or arises or deemed to accrue or arise, directly or indirectly, through or from any source in India from liaison offices within the meaning of section 5 or section 9 of the Income-tax Act, 1961 (for short, "the 1961 Act"). According to the respondent, the remittance services are offered by the respondent to non-resident Indians (for short, "NRIs") in UAE. The contract pursuant to which the funds are handed over by the NRI to the respondent in UAE, is entered into between the respondent and the NRI remitter in UAE. The funds are collected from the NRI remitter by the respondent in UAE by charging one-time fee of Dirhams 15. After

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collecting the funds from the NRI remitter, the respondent makes an electronic remittance of the funds on behalf of its NRI customer in two ways :

(i) by telegraphic transfer through bank channels ; or

(ii) On the request of the NRI remitter, the respondent sends instruments/cheques through its liaison offices to the beneficiaries in India, designated by the NRI remitter.

The dispute arises in respect of the second mode of remittance through the liaison offices in India. That is on account of the activity undertaken in the liaison office in India of downloading the particulars of remittances through electronic media and printing cheques/drafts drawn on the banks in India, which, in turn, are couriered or dispatched to the beneficiaries in India, in accordance with the instructions of the NRI remitter. While doing this, the liaison office of the respondent remains connected with its main server in UAE, as the information is contained in the main server thereat, which could be accessed by the liaison office in India for the purpose of remittance of funds to the beneficiaries in India by the NRI remitters.

3

It is stated that, in compliance with section 139 of the 1961 Act, the respondent had been filing its returns of income, since the assessment year 1998-99 until 2003-04, showing nil income, as according to the respondent, no income had accrued or deemed to have accrued to it in India, both under the 1961 Act, as well as, the agreement entered into between the Government of the Republic of India and the Government of the UAE, which is known as Double Taxation Avoidance Agreement (for short, "DTAA"). This agreement (DTAA) has been entered into between the two sovereign countries in exercise of powers under section 90 of the 1961 Act, for the purpose of avoidance of double taxation and prevention of fiscal evasion, with respect to taxes and income on capital. The double taxation avoidance agreement has been notified vide Notification No. G. S. R. No. 710(E), dated November 18, 1993[1]. As noted earlier, returns were filed on regular basis by the respondent, which were accepted by the Department without any demur. However, as some doubt was entertained, the respondent filed an application under section 245Q(1) of the 1961 Act before the Authority for Advance Rulings (Income-tax), New Delhi (for short, "the Authority"), which was numbered as AAR No. 608 of 2003[2] and sought ruling of the authority on the following question :

> "Whether any income is accrued/deemed to be accrued in India from the activities carried out by the Company in India ?"

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1. [1994] 205 ITR (St.) 49.
2. UAE Exchange Centre LLC, *In re* [2004] 268 ITR 9 (AAR).

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The authority, vide its ruling dated May 26, 2004 answered the question in the affirmative, namely, "Income shall be deemed to accrue in India from the activity carried out by the liaison offices of the applicant in India". For so holding, the authority opined that in view of the deeming provisions in sections 2(24), 4 and 5 read with section 9 of the 1961 Act, the respondent-assessee would be liable to pay tax under the 1961 Act, as it had carried on business in India through a "permanent establishment" (for short, "PE") situated in India and the profits of the enterprise needed to be taxed in India, but only so much of that, as is attributable to the liaison offices in India (permanent establishment). The authority, amongst others, first examined the facts of the case to ascertain as to whether any income accrues/arises or is deemed to accrue/arise to the respondent in India under sections 2(24), 5(2) and 9(1)(i) of the 1961 Act. It noted that the business of the respondent was being carried on in UAE ; a contract for remitting the amounts is entered into with NRIs and is executed outside India ; and even the commission for remitting the amounts is also earned by the respondent outside India, therefore, ostensibly no income accrues/arises, or is deemed to accrue or arise in India. It then adverted to *Explanation* to section 9(1)(i) and observed that all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or from any property in India, or through any assets or source of income in India or through transfer of capital assets situate in India, shall be deemed to accrue in India. It went on to observe that in the present case, it was evident that all the operations of the business of the respondent were not carried out in India. In such a situation, to attract the provisions referred to above, it must be shown that — (i) the applicant has "business connections" in India ; and (ii) the income of the business can be deemed to accrue or arise in India from such operations, as are carried out in India. After analysing this aspect and *Explanation 2* to section 9(1)(i) inserted by the Finance Act, 2003, it noted the decision of this court in *CIT* v. *R. D. Aggarwal and Company*[1] and culled out the essential features of expression "business connection" as follows[2] :

> "In the light of above discussion, the essential features of 'business connection' may be summed up as follows :
>
> (a) a real and intimate relation must exist between the trading activities by a non-resident carried on outside India and the activities within India ;

1. [1965] 56 ITR 20 (SC) ; AIR 1965 SC 1526.
2. Page 16 of 268 ITR.

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(b) the relation contributes directly or indirectly to the earning of income by the non-resident in his business ;

(c) a course of dealing or continuity of relationship and not a mere isolated or stray nexus between the business of the non-resident outside India and the activity in India, would furnish a strong indication of business connection."

It then observed in paragraph 11 of the ruling, as follows[1] :

"Admittedly, the applicant is having liaison offices in India. They attend to the complaints of the clients in cases where remittances are sent directly to banks in India UAE. In addition, in cases where the applicant has to remit the amounts to the beneficiaries in India, as per the directions of the NRIs, the liaison offices download the information from the internet, print cheques/drafts in the name of the beneficiaries in India send them through couriers to various places in India. Without the latter activity, the transaction of remittance of the amounts in terms of the contract with the NRIs would not be complete. The commission which the applicant receives for remitting the amount covers not only the business activities carried on in UAE but also the activity of remittance of the amount to the beneficiary in India by cheques/drafts through courier which is being attended to by the liaison offices. There is, therefore, a real relation between the business carried on by the applicant for which it receives commission in UAE and the activities of the liaison offices downloading of information, printing and preparation of cheques/drafts and sending the same to the beneficiaries in India, which contributes directly or indirectly to the earning of the income by the applicant by way of commission. There is also continuity between the business of the applicant in UAE and the activities carried on by the liaison offices. Therefore, it follows that income shall be deemed to accrue/arise to the applicant in UAE from 'business connection' in India. However, the deemed accrual of income to the applicant from the business connection in India in view of *Explanation 1* would be only such part of the income as is reasonably attributable to the operations which are carried out in India."

The authority also took note of articles 5 and 7 of double taxation avoidance agreement and then noted in paragraph 14 as follows[2] :

". . . The moot question is whether the exclusionary clause (e) of para 3 is attracted ; if so, whether the liaison offices would stand

1. Page 16 of 268 ITR.
2. Page 18 of 268 ITR.

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excluded from the meaning of the expression 'permanent establishment'. Clause (e) of para 3 says that the expression 'permanent establishment' shall be deemed not to include the maintaining of a fixed place of business solely for the purpose of carrying on for an enterprise any other activity of a preparatory or auxiliary character. Mr. Ranina placed before us extracts from various dictionaries to show the meaning of the word 'auxiliary'. It is unnecessary to refer to them here. Suffice it to say that the word 'auxiliary' in common English usage means helping, assisting or supporting the main activity. We have, therefore, to ascertain whether the activities carried on in the liaison offices in India, are only supportive of the main business or form one of the main functions of the business. The applicant enters into a contract with an NRI to remit to the nominated banks or the nominated beneficiaries in India the amount which is the Indian rupee equivalent of foreign currency handed over to it. It is true that the contract is entered into in UAE and the amount to be remitted as well as the commission is also received in UAE. The contract is, therefore executed in UAE. To fulfill its obligation under the contract the applicant remits the amount in either of the following two modes :

By establishment in UAE—

(i) by telegraphic instructions from Abu Dhabi through banking channels or by liaison offices in India—

(ii) by dispatching through courier the instruments of cheques/drafts prepared by liaison offices to the beneficiaries at various places in India.

In so far as the first mode is concerned, the amount is remitted telegraphically by transferring directly from UAE through bank channel to various places in India and in such remittances the liaison offices have no role to play except attending to the complaints, if any, in India regarding the remittances in cases of fraud, etc. This is undoubtedly a work of auxiliary character. However, where the applicant adopts the second mode for remitting the amounts in India-an activity approved by the RBI — the liaison offices of the applicant play an important role. They download the data from internet with regard to the amount to be remitted, the names and addresses of the beneficiaries and then print cheques/drafts and dispatch them to the addresses of the beneficiaries in India through courier. The role of liaison offices in remitting the amounts by adopting the second mode, is nothing short of performing the contract of remitting the amounts at least in part. This case presents a good example of an auxiliary

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activity to the main activities and an essential activity in performance of contractual obligation. Whereas in the first mode, the activity undertaken by the liaison offices in India may be said to be auxiliary in character, the same cannot be said of the second mode. Downloading the data, preparing cheques for remitting the amount, dispatching the same through courier by the liaison offices is an important part of the main work itself because without remitting the amount to the beneficiaries as desired by the NRIs, performance of the contract will not be complete. So the activities of the liaison offices in the second mode remittance, cannot be said to be work of auxiliary character. It is indeed a significant part of the main work of UAE establishment. It follows that the liaison offices of the applicant in India for the purposes of the second mode of remittance of amount would be a 'permanent establishment' within the meaning of the expression in double taxation avoidance agreement."

The authority accordingly concluded that so much of the profits as shall be deemed to accrue or arise to the respondent in India, which were attributable to the permanent establishment, namely, the liaison offices in India, would be taxable in India even under the double taxation avoidance agreement, and answered the question affirmatively against the respondent-assessee.

4 Following the impugned ruling of the authority, dated May 26, 2004, the Department issued four notices of even date, i.e., July 19, 2004 under section 148 of the 1961 Act addressed to the respondent pertaining to the assessment years 2000-01, 2001-02, 2002-03 and 2003-04 respectively. The respondent, therefore, carried the matter before the High Court of Delhi at New Delhi (for short, "the High Court") by way of Writ Petition No. 14869 of 2004[1], inter alia, for quashing of the ruling of the authority dated May 26, 2004, quashing of stated notices and for a direction to the appellants not to tax the respondent in India because no income had accrued to it or is deemed to have accrued to it in India from its activities of liaison offices in India. The High Court, after adverting to indisputable facts, noted that the authority committed manifest error in appreciating the relevant facts and materials on record and more particularly, misread the purport of section 90 of the 1961 Act and the settled legal position that the double taxation avoidance agreement ought to override the provisions of the Act (the 1961 Act). In other words, the tax liability of the respondent was required to be assessed on the basis of the provisions in the stated treaty, namely, double taxation avoidance agreement. The High Court adverted to the exposition

1. *U. A. E. Exchange Centre Ltd.* v. *Union of India* [2009] 313 ITR 94 (Delhi).

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in *Union of India* v. *Azadi Bachao Andolan*[1] in paragraphs 28 and 29 and then observed as follows[2] :

> "In the present case, the liability to tax under the double taxation avoidance agreement is governed by article 7. Sub-section (1) of article 7 of the double taxation avoidance agreement categorically provides that profits of an enterprise of a Contracting State shall be taxable only in that State, unless the enterprise carries on business, in the other State, through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other State, but only so much of that, as is attributable to the permanent establishment. Therefore, the liability on account of tax, of an enterprise of either of the Contracting States, in India, would arise if the enterprise in issue, i.e., the petitioner, had a permanent establishment in India. The provisions of section 5(2)(b) and section 9(1)(i) of the Act would have, in our view, no applicability. Discussion with respect to the 'business connection' in the impugned ruling was, in our view, unnecessary. The authority had to determine only whether the petitioner carried on business in India through a permanent establishment. For this purpose it was required to examine the definition of permanent establishment as contained in article 5 of double taxation avoidance agreement read with article 5(3)(e). There is no dispute raised by the petitioner that it maintains liaison offices in India and hence, would fall within the definition of permanent establishment in accordance with the provisions of article 5(2)(c). The petitioner, however, has contended both before the authority and before us that it falls within the exclusionary clause contained in article 5(3)(e) inasmuch as the activity carried on by the liaison offices in India, has an 'auxiliary' character. On this aspect of the matter the discussion and reasoning by the Authority is contained in paragraphs 12 to 15 of the impugned ruling. The Authority came to the conclusion that the activity carried on by the liaison offices in India did not have an 'auxiliary' character in terms of article 5(3)(e) of the Act as the option of remitting of funds through the liaison offices in India was exercised by the NRI remitter which was 'nothing short of, as in the words of the parties, performing contract of remitting the amounts'. The Authority, thus, held that while, in respect of all remittances of funds by telegraphic transfer through banking channels, the role of the liaison offices in India of an

1. [2003] 263 ITR 706 (SC) ; [2004] 10 SCC 1.
2. Page 110 of 313 ITR.

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> 'auxiliary' character, the same was not true in respect of remittance of funds through liaison offices in India. This was based on the reasoning that without remittances of funds to the beneficiaries in India performance under the contract would not have been complete and thus, the downloading of data, preparation of cheques for remitting the amount, dispatching the same through courier by the liaison offices, constituted an important part of the main work, which was, remitting the amount to the beneficiaries as desired by the NRIs. Based on this reasoning, the Authority came to the conclusion that the work of the liaison offices in India, being a significant part of the main work of UAE establishment, the liaison office of the petitioner, in India, would constitute a 'permanent establishment' within the provisions of the double taxation avoidance agreement."

And again, whilst analysing the scope of articles 5 and 7 of the double taxation avoidance agreement in paragraph 12 of the impugned judgment, the High Court noted thus[1] :

> "In the case of double taxation avoidance agreement under consideration in the present case under article 5 read with article 7, profits of an enterprise are liable to tax in India if an enterprise were to carry on business through a permanent establishment, meaning thereby fixed place of business through which business of an enterprise is wholly or partly carried on. Under article 5(2)(c), amongst others, permanent establishment includes an office. However, article 5(3) which opens with a non obstante clause, is illustrative of instances where under the double taxation avoidance agreement various activities have been deemed as ones which would not fall within the ambit of the expression 'permanent establishment'. One such exclusionary clause is found in article 5(3)(e) which is : maintenance of fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character. The plain meaning of the word 'auxiliary' is found in *Black's Law Dictionary* 7th Edition at page 130 which reads as 'aiding or supporting, subsidiary'. The only activity of the liaison offices in India is simply to download information which is contained in the main servers located in UAE based on which cheques are drawn on banks in India whereupon the said cheques are couriered or dispatched to the beneficiaries in India, keeping in mind the instructions of the NRI remitter. Can such an activity be anything but auxiliary in character. Plainly to our minds, the instant activity is in 'aid' or 'support' of the main activity.

1. Page 111 of 313 ITR.

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The error into which, according to us, the authority has fallen is in reading article 5(3)(e) as a clause which permits making a value judgment as to whether the transaction would or would not have been complete till the role played by liaison offices in India was fulfilled as represented by the petitioner to their NRI remitter. According to us, what has been lost sight of, is that, by invoking the clause with regard to permanent establishment, we would, by a deeming fiction tax an income which otherwise neither arose nor accrued in India – when looked at from this point of view, the exclusionary clause contained in article 5(3) and in this case in particular, sub-clause (e) have to be given a wider and liberal play. Once an activity is construed as being subsidiary or in aid or support of the main activity it would, according to us, fall within the exclusionary clause. To say that a particular activity was necessary for completion of the contract is, in a sense saying the obvious as every other activity which an enterprise undertakes in earning profits is with the ultimate view of giving effect to the obligations undertaken by an enterprise vis-a-vis its customer. If looked at from that point of view, then, no activity could be construed as preparatory or of an 'auxiliary' character. On this aspect of the matter, the Supreme Court in the case of *DIT (International Taxation)* v. *Morgan Stanley and Co. Inc.* [2007] 7 SCC 1[1] amongst other issues was called upon to decide as to whether back office operations carried on by Morgan Stanley Company for one of its Morgan Stanley Advantages Services Pvt. Ltd. would qualify as having a permanent establishment in India. The Supreme Court, while holding that back office operations fall within the exclusionary clause article 5(3)(e) of Indo-US DTAA, which is, identical to double taxation avoidance agreement under consideration in the present case, came to the conclusion that back office operations came within the purview of article 5(3)(e). It is laid down by the Supreme Court in the case of *Morgan Stanley* (supra) that in ascertaining what would constitute a 'permanent establishment' within the meaning of article 5(1) of the Indo-US DTAA, one had to undertake what is called a functional and factual analysis of each of the activities undertaken by an establishment. In that case the Supreme Court came to the conclusion that the entity located in India which was engaged in only supporting the front office functions of Morgan Stanley and Co., a non-resident, in fixed income and equity research and information technology enabled services such as data processing support centre, technical services and

1. [2007] 292 ITR 416 (SC).

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> reconciliation of accounts being back office operators would not fall within article 5(1) of the Indo-US DTAA."

Accordingly, the High Court was of the opinion that the authority proceeded on a wrong premise by first examining the efficacy of section 5(2)(b) and section 9(1)(i) of the 1961 Act instead of applying the provisions in articles 5 and 7 of the double taxation avoidance agreement for ascertaining the respondent's liability to tax. Further, the nature of activities carried on by the respondent-assessee in the liaison offices being only of preparatory and auxiliary character, were clearly excluded by virtue of the deeming provision. The High Court distinguished the decisions relied upon by the authority in *Anglo-French Textile Co. Ltd.* v. *CIT*[1] and *R. D. Aggarwal and Company* (supra). Inasmuch as, the ratio in these decisions, according to the High Court, was that the non-resident entity could be taxed only if there was business connection between the business carried on by a non-resident which yields profits or gains and some activity in the taxable territory which contributes directly or indirectly to the earning of those profits or gains. The High Court then concluded that the activity carried by the liaison offices of the respondent in India did not in any manner contribute directly or indirectly to the earning of profits or gains by the respondent in UAE and more so, every aspect of the transaction was concluded in UAE, whereas, the activity performed by the liaison offices in India was only supportive of the transaction carried on in UAE. The High Court also took note of *Explanation 2* to section 9(1)(i) and observed that the same reinforces the fact that in order to have a business connection, in respect of a business activity carried on by non-resident through a person situated in India, it should involve more than what is supportive or subsidiary to the main function referred to in clauses (a) to (c). The High Court eventually quashed the impugned ruling of the authority and also the notices issued by the Department under section 148 of the 1961 Act, since the notices were based on the ruling which was being set aside. The High Court, however, gave liberty to the appellants to proceed against the respondent on any other ground, as may be permissible in law.

5 Feeling aggrieved, the Department has assailed the decision of the High Court by way of the present appeal arising from SLP(C) No. 31276 of 2011.

6 We have heard Mr. Arijit Prasad, learned senior counsel for the appellants and Mr. H.P. Ranina, learned counsel for the respondent.

7 Both sides have more or less reiterated the stand taken before the authority and the High Court. After cogitating over the rival submissions

1. [1953] 23 ITR 101 (SC) ; [1953] AIR 1953 SC 105.

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and the opinion recorded by the authority and the High Court, the core issue that needs to be answered in this appeal is : whether the stated activities of the respondent-assessee would qualify the expression "of preparatory or auxiliary character"? Having regard to the nature of activities carried on by the respondent-assessee, as held by the authority, it would appear that the respondent was engaged in "business" and had "business connections", for which, by virtue of deeming provision and the sweep of sections 2(24), 4 and 5 read with section 9 of the 1961 Act including the exposition in *Anglo-French Textile Co. Ltd.* (supra) and *R. D. Aggarwal and Company* (supra), it would be a case of income deemed to accrue or arise in India to the respondent.

8 However, in the present case, the matter in issue will have to be answered on the basis of the stipulations in double taxation avoidance agreement notified in exercise of powers conferred under section 90 of the 1961 Act. This position is no more res integra in view of the dictum in *Azadi Bachao Andolan* (supra). The efficacy of section 90 of the 1961 Act has been delineated by this court after adverting to the decisions in *CIT* v. *Vishakhapatnam Port Trust*[1], *CIT* v. *Davy Ashmore India Ltd.*,[2] *Leonhardt Andra Und Partner, GmbH* v. *CIT*[3], *CIT* v. *R. M. Muthaiah*[4] and *Arabian Express Line Ltd. of United Kingdom* v. *Union of India*[5], whereafter the court went on to observe in paragraph 28, as follows[6] :

> "A survey of the aforesaid cases makes it clear that the judicial consensus in India has been that section 90 is specifically intended to enable and empower the Central Government to issue a notification for implementation of the terms of a Double Taxation Avoidance Agreement. *When that happens, the provisions of such an agreement, with respect to cases to which they apply, would operate even if inconsistent with the provisions of the Income-tax Act.* We approve of the reasoning in the decisions which we have noticed. If it was not the intention of the Legislature to make a departure from the general principle of chargeability to tax under section 4 and the general principle of ascertainment of total income under section 5 of the Act, then there was no purpose of making those sections 'subject to the provisions' of the Act. The very object of grafting the said two sections

1. [1983] 144 ITR 146 (AP).
2. [1991] 190 ITR 626 (Cal).
3. [2001] 249 ITR 418 (Cal).
4. [1993] 202 ITR 508 (Karn)
5. [1995] 212 ITR 31 (Guj).
6. Page 724 of 263 ITR.

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with the said clause is to enable the Central Government to issue a notification under section 90 towards implementation of the terms of DTACs which would automatically override the provisions of the Income-tax Act in the matter of ascertainment of chargeability to income-tax and ascertainment of total income, to the extent of inconsistency with the terms of DTAC." (emphasis[1] supplied)

In view of this exposition, which squarely applies to the fact situation of the present case, we must answer the question under consideration in light of the purport of provisions in double taxation avoidance agreement, which has been executed by the Government of India and the Government of UAE, and has come into force consequent to publication vide notification dated November 18, 1993[2]. The recitals of the said notification read thus :

"Income-tax Act, 1961 : Notification under section 90 : Agreement between the Government of the Republic of India and the Government of the United Arab Emirates for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and on capital

Notification G. S. R. No. 710(E), dated 18th November, 1993

Whereas the annexed agreement between the Government of the United Arab Emirates and the Government of the Republic of India for the avoidance of double taxation and prevention of fiscal evasion with respect to taxes on income and on capital has entered into force on September 22, 1993, after the notification by both the Contracting States to each other of the completion of the proceedings required by laws for bringing into force of the said agreement in accordance with paragraph 1 of article 30 of the said Agreement :

Now, therefore, in exercise of the powers conferred by section 90 of the Income-tax Act, 1961 (43 of 1961), section 24A of the Companies (Profits) Surtax Act, 1964 (7 of 1964), and section 44A of the Wealth-tax Act, 1957 (27 of 1957), the Central Government hereby directs that all the provisions of the said agreement shall be given effect to in the Union of India.

Annexure

An agreement between the Government of the Republic of India and the Government of the United Arab Emirates for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and on capital.

1. Here printed in italics.
2. [1994] 205 ITR (St.) 49.

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The Government of the Republic of India and the Government of the United Arab Emirates

Desiring to promote mutual economic relations by concluding an Agreement for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and on capital.

Have agreed as follows :"

Article 1 of the double taxation avoidance agreement bears title "Personal Scope" predicating that the agreement shall apply to persons who are residents of one or both of the Contracting States. Article 2 deals with "Taxes Covered", to which the agreement would apply. Article 2 reads thus :[1]

"*Article 2*

TAXES COVERED

1. There shall be regarded as taxes on income and on capital all taxes imposed on total income, on total capital, or on elements of income or of capital including taxes on gains from alienation of movable or immovable property as well as on capital appreciation.

2. The existing taxes to which the Agreement shall apply are :

(a) In United Arab Emirates :

(i) Income-tax ;

(ii) Corporation tax ;

(iii) Wealth-tax

(hereinafter referred to as 'U.A.E. tax') ;

(b) In India :

(i) the income-tax including any surcharge thereon ;

(ii) the surtax ; and

(iii) the wealth-tax

(hereinafter referred to as 'Indian tax').

3. This Agreement shall also apply to any identical or substantially similar taxes on income or capital which are imposed at Federal or State level by either Contracting State in addition to, or in place of, the taxes referred to in paragraph 2 of this Article. The competent authorities of the Contracting States shall notify each other of any substantial changes which are made in their respective taxation laws."

Article 3 refers to General Definitions and the meaning of the concerned expression contained in the agreement, unless the context otherwise requires. Article 4 pertains to "Resident of the Contracting State". The other articles which may have bearing on the question posed before us are

1. Page 50 of 205 ITR (St.).

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Articles 5 and 7, dealing with "Permanent Establishment (PE)" and "Business Profits" respectively, which read thus[1] :

"*Article 5*

PERMANENT ESTABLISHMENT

1. For the purposes of this Agreement, the term 'permanent establishment' means a fixed place of business through which the business of an enterprise is wholly or partly carried on.

2. The term 'permanent establishment' includes especially :

(a) a place of management ;

(b) a branch ;

(c) an office ;

(d) a factory ;

(e) a workshop ;

(f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources ;

(g) a farm or plantation ;

(h) a building site or construction or assembly project or supervisory activities in connection therewith, but only where such site, project or activity continues for a period of more than 9 months ;

(i) the furnishing of services including consultancy services by an enterprise of a Contracting State through employees or other personnel in the other Contracting State, provided that such activities continue for the same project or connected project for a period or periods aggregating to more than 9 months within any twelve-month period.

(3) Notwithstanding the preceding provisions of this article, the term 'permanent establishment' shall be deemed not to include :

(a) the use of facilities solely for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise ;

(b) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display or delivery ;

(c) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise ;

(d) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise, or of collecting information, for the enterprise ;

1. Pages 52 and 54 of 205 ITR (St.).

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(e) the maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character.

4. Notwithstanding the provisions of paragraphs 1 and 2, where a person — other than an agent of independent status to whom paragraph 5 applies — is acting on behalf of an enterprise and has, and habitually exercises in a Contracting State an authority to conclude contracts on behalf of the enterprise, that enterprise shall be deemed to have a permanent establishment in that State in respect of any activities which that person undertakes for the enterprise, unless the activities of such persons are limited to the purchase of goods or merchandise for the enterprise.

5. An enterprise of a Contracting State shall not be deemed to have a permanent establishment in the other Contracting State merely because it carries on business in that other State through a broker, general commission agent or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business. However, when the activities of such an agent are devoted wholly or almost wholly on behalf of that enterprise, he will not be considered an agent of an independent status within the meaning of this paragraph.

Article 7

BUSINESS PROFITS

1. The profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to that permanent establishment.

2. Subject to the provisions of paragraph 3, where an enterprise of a Contracting State carries on business in the other Contracting State through a permanent establishment situated therein, there shall in each Contracting State be attributed to that permanent establishment the profits which it might be expected to make if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a permanent establishment.

3. In determining the profits of a permanent establishment, there shall be allowed as deductions expenses which are incurred for the

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purposes of the business of the permanent establishment, including executive and general administrative expenses so incurred, whether in the State in which the permanent establishment is situated or elsewhere.

4. In so far as it has been customary in a Contracting State to determine the profits to be attributed to a permanent establishment on the basis of an apportionment of the total profits of the enterprise to its various parts, nothing in paragraph 2 shall preclude that Contracting State from determining the profits to be taxed by such an apportionment as may be customary ; the methods of apportionment adopted shall, however, be such that, the result shall be in accordance with the principles contained in this article.

5. No profits shall be attributed to a permanent establishment by reason of the mere purchase by the permanent establishment of goods or merchandise for the enterprise.

6. For the purposes of the preceding paragraphs, the profits to be attributed to the permanent establishment shall be determined by the same method year by year unless there is good and sufficient reason to the contrary.

7. Where profits include items of income which are dealt with separately in other articles of this agreement, then the provisions of those articles shall not be affected by the provisions of this article."

Keeping in view the finding recorded by the High Court, we may proceed on the basis that the respondent-assessee had a fixed place of business through which the business of the respondent was being wholly or partly carried on. That, however, would not be conclusive until a further finding is recorded that the respondent had a permanent establishment situated in India, so as to attract article 7 dealing with business profits to become taxable in India, to the extent attributable to the permanent establishment of the respondent in India. For that, we may have to revert back to article 5, which deals with and defines the "permanent establishment (PE)". A fixed place of business through which the business of an enterprise is wholly or partly carried on is regarded as a permanent establishment. The term "permanent establishment (PE)" would include the specified places referred to in clause 2 of article 5. It is not in dispute that the place from where the activities are carried on by the respondent in India is a liaison office and would, therefore, be covered by the term permanent establishment in article 5(2). However, article 5(3) of the double taxation avoidance agreement opens with a non obstante clause and also contains a deeming provision. It predicates that notwithstanding the

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preceding provisions of the concerned article, which would mean clauses 1 and 2 of article 5, it would still not be a permanent establishment, if any of the clauses in article 5(3) are applicable. For that, the functional test regarding the activity in question would be essential. The High Court has opined that the respondent was carrying on stated activities in the fixed place of business in India of a preparatory or auxiliary character. Indeed, the expression "business" has been defined in the 1961 Act, as follows :

> "2. *Definitions.*—In this Act, unless the context otherwise requires,— . . .
>
> (13) 'business' includes any trade, commerce or manufacture or any adventure or concern in the nature of trade, commerce or manufacture ;"

The expression "business connection" can be discerned from section 9(1), as also, the meaning of expression "business activity". We will advert to those provisions a little later and for the time being, assume that the stated activities of the respondent are business activities. However, since the stated activities of the liaison offices of the respondent in India are of preparatory or auxiliary character, the same would fall within the excepted category under article 5(3)(e) of the double taxation avoidance agreement. Resultantly, it cannot be regarded as a permanent establishment within the sweep of article 7 of double taxation avoidance agreement. The expression "preparatory" is not defined in the 1961 Act or the double taxation avoidance agreement. The dictionary meaning of that expression can be traced to term "preparatory work" and "travaux préparatoires", which in the *Black's Law Dictionary* (Eleventh Edition), read thus :

> "preparatory work. See Travaux Préparatoires.
>
> travaux préparatoires. Materials used in preparing the ultimate form of an agreement or statute, and esp. of an international treaty ; the draft or legislative history of a treaty."

The expression "auxiliary" is also not defined in the 1961 Act or the double taxation avoidance agreement. In common parlance, the meaning of that expression is predicated in *Concise Oxford English Dictionary* (Twelfth Edition), which reads thus :

> "Auxiliary adj. providing additional help or support. n. an auxiliary person or thing. N. Amer. A group of volunteers who assist a church, hospital, etc., with charitable activities."

In *Black's Law Dictionary* (Eleventh Edition), the term "auxiliary" is defined as follows :

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"Auxiliary adj. 1. Aiding or supporting. 2. Subsidiary. 3. Supplementary."

The crucial activities in the present case are of downloading particulars of remittances through electronic media and then printing cheques/drafts drawn on the banks in India, which, in turn, are couriered or dispatched to the beneficiaries in India, in accordance with the instructions of the NRI remitter. While doing so, the liaison office of the respondent in India remains connected with its main server in UAE and the information residing thereat is accessed by the liaison office in India for the purpose of remittance of funds to the beneficiaries in India by the NRI remitters. These are combination of virtual and physical activities unlike the virtual activity of funds being remitted by telegraphic transfer through banking channels. As regards the latter, it is not the case of the Department that the same would be covered and amenable to tax liability by virtue of deeming provision in the 1961 Act.

9

While answering the question as to whether the activity in question can be termed as other than that "of preparatory or auxiliary character", we need to keep in mind the limited permission given by the RBI to the respondent under section 29(1)(a) of the 1973 Act, on September 24, 1996. From paragraph 2 of the stated permission, it is evident that the RBI had agreed for establishing a liaison office of the respondent at Cochin, initially for a period of three years to enable the respondent to (i) respond quickly and economically to enquiries from correspondent banks with regard to suspected fraudulent drafts ; (ii) undertake reconciliation of bank accounts held in India ; (iii) act as a communication centre receiving computer (via modem) advices of mail transfer T. T. stop payments messages, payment details, etc., originating from respondent's several branches in UAE and transmitting to its Indian correspondent banks ; (iv) printing Indian Rupee drafts with facsimile signature from the Head Office and counter signature by the authorised signatory of the Office at Cochin ; and (v) following up with the Indian correspondent banks. These are the limited activities which the respondent has been permitted to carry on within India. This permission does not allow the respondent-assessee to enter into a contract with anyone in India, but only to provide service of delivery of cheques/drafts drawn on the banks in India. Notably, the permitted activities are required to be carried out by the respondent subject to conditions specified in clause 3 of the permission, which includes not to render any consultancy or any other service, directly or indirectly, with or without any consideration and further that the liaison office in India shall not borrow or lend any money from or to any person in India without prior permission of RBI. The

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conditions make it amply clear that the office in India will not undertake any other activity of trading, commercial or industrial, nor shall it enter into any business contracts in its own name without prior permission of the RBI. The liaison office of the respondent in India cannot even charge commission/fee or receive any remuneration or income in respect of the activities undertaken by the liaison office in India. From the onerous stipulations specified by the RBI, it could be safely concluded, as opined by the High Court, that the activities in question of the liaison office(s) of the respondent in India are circumscribed by the permission given by the RBI and are in the nature of preparatory or auxiliary character. That finding reached by the High Court is unexceptionable.

10 The High Court had justly adverted to the exposition of this court in *DIT (International Taxation)* v. *Morgan Stanley and Co. Inc.*[1], which dealt with the case of an assessee having set up office in India to support the main office functions in fixed income and equity research and in providing IT enabled services such as back office operations, data processing and support centres to the entity in United States. This court, in paragraphs 10 to 14, observed thus[2] :

> "In our view, the second requirement of article 5(1) of double taxation avoidance agreement is not satisfied as regards back office functions. We have examined the terms of the Agreement along with the advance ruling application made by MSCo inviting authority for advance rulings to give its ruling. It is clear from reading of the above agreement/application that MSAS in India would be engaged in supporting the front office functions of MSCo in fixed income and equity research and in providing IT enabled services such as data processing support centre and technical services as also reconciliation of accounts. *In order to decide whether a permanent establishment stood constituted one has to undertake what is called as a functional and factual analysis of each of the activities to be undertaken by an establishment.* It is from that point of view, we are in agreement with the ruling of authority for advance ruling that in the present case article 5(1) is not applicable as the said MSAS would be performing in India only back office operations. Therefore to the extent of the above back office functions the second part of article 5(1) is not attracted.
>
> *Lastly, as rightly held by authority for advance ruling there is no agency permanent establishment as the permanent establishment in India had no authority to enter into or conclude contracts. The*

1. [2007] 292 ITR 416 (SC) ; [2007] 7 SCC 1.
2. Page 425 of 292 ITR.

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contracts would be entered into in the United States. They would be concluded in US. The implementation of those contracts only to the extent of back office functions would be carried out in India, and therefore, MSAS would not constitute an agency permanent establishment as contended on behalf of the Department.

In the double taxation avoidance agreement, the term permanent establishment means a fixed place of business through which the business of an MNE is wholly or partly carried out. The definition of the word permanent establishment in section 92F(iii) is inclusive, however, it is not under article 5(1) of the Treaty. It is for this reason that article 5(2) of double taxation avoidance agreement herein refers to places included as permanent establishment of the MNE. One such place is mentioned in article 5(2)(i) which deals with furnishing of services.

The concept of permanent establishment was introduced in the 1961 Act as part of the statutory provisions of transfer pricing by the Finance Act of 2001. In section 92F(iii) the word 'enterprise' is defined to mean—'a person including a permanent establishment of such person who is, or has been, or is proposed to be, engaged in any activity, relating to the production'. Under CBDT Circular No. 14 of 2001[1] it has been clarified that the term permanent establishment has not been defined in the Act but its meaning may be understood with reference to double taxation avoidance agreement entered into by India. Thus the intention was to rely on the concept and definition of permanent establishment in double taxation avoidance agreement. However, vide the Finance Act, 2002 the definition of permanent establishment was inserted in the Income-tax Act, 1961 (for short "the IT Act") vide section 92F(iiia) which states that the permanent establishment shall include a fixed place of business through which the business of MNE is wholly or partly carried on. *This is where the difference lies between the definition of the word permanent establishment in the inclusive sense under the Income-tax Act as against the definition of the word permanent establishment in the exhaustive sense under double taxation avoidance agreement. This analysis is important because it indicates the intention of Parliament in adopting an inclusive definition of permanent establishment so as to cover service permanent establishment, agency permanent establishment, software permanent establishment, construction permanent establishment*, etc.

1. [2001] 252 ITR (St.) 65, 107.

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There is one more aspect which needs to be discussed, namely, exclusion of permanent establishment under article 5(3). Under article 5(3)(e) activities which are preparatory or auxiliary in character which are carried out at a fixed place of business will not constitute a permanent establishment. Article 5(3) commences with a non obstante clause. It states that notwithstanding what is stated in article 5(1) or under article 5(2) the term permanent establishment shall not include maintenance of a fixed place of business solely for advertisement, scientific research or for activities which are preparatory or auxiliary in character. In the present case we are of the view that the abovementioned back office functions proposed to be performed by MSAS in India falls under article 5(3)(e) of double taxation avoidance agreement. Therefore, in our view in the present case MSAS would not constitute a fixed place permanent establishment under article 5(1) of double taxation avoidance agreement as regards its back office operations." (emphasis[1] supplied)

Learned counsel for the appellant, however, attempted to distinguish this judgment on the argument that this case dealt with the issue of service permanent establishment. According to him, the court must examine the full transactions of the respondent to determine whether the work done by the respondent-assessee was one of a backup office work or auxiliary work. In so far as the nature of activities carried on by the respondent through the liaison office in India, as permitted by the RBI, we have upheld the conclusion of the High Court that the same were in the nature of "preparatory or auxiliary character" and, therefore, covered by article 5(3)(e). As a result, the fixed place used by the respondent as liaison office in India, would not qualify the definition of permanent establishment in terms of articles 5(1) and 5(2) of the double taxation avoidance agreement on account of non obstante and deeming clause in article 5(3) of the Double Taxation Avoidance Agreement.

11 Having said thus, it must follow that the respondent was not carrying on any business activity in India as such, but only dispensing with the remittances by downloading information from the main server of the respondent in UAE and printing cheques/drafts drawn on the banks in India as per the instructions given by the NRI remitters in UAE. The transaction(s) had completed with the remitters in UAE, and no charges towards fee/commission could be collected by the liaison office in India in that regard. To put it differently, no income as specified in section 2(24) of the 1961 Act is

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earned by the liaison office in India and moreso because, the liaison office is not a permanent establishment in terms of article 5 of double taxation avoidance agreement (as it is only carrying on activity of a preparatory or auxiliary character). The concomitant is - no tax can be levied or collected from the liaison office of the respondent in India in respect of the primary business activities consummated by the respondent in UAE. The activities carried on by the liaison office of the respondent in India as permitted by the RBI, clearly demonstrate that the respondent must steer away from engaging in any primary business activity and in establishing business connection as such. It can carry on activities of preparatory or auxiliary nature only. In that case, the deeming provisions in sections 5 and 9 of the 1961 Act can have no bearing whatsoever.

12 Our attention was invited to the dictum in *Asst. DIT* v. *E-Funds IT Solution Inc.*[1]. Paragraph 2 of the said decision would clearly indicate the background in which the issue was answered by this court. The same reads thus[2] :

> "The assessing authority decided that the assessees had a permanent establishment (hereinafter referred to as 'PE') as they had a fixed place where they carried on their own business in Delhi, and that, consequently, article 5 of the India-US Double Taxation Avoidance Agreement of 1990 (hereinafter referred to as 'DTAA') was attracted. Consequently, the assessees were liable to pay tax in respect of what they earned from the aforesaid fixed place permanent establishment in India. The Commissioner of Income (Appeals) dismissed the appeals of the assessees holding that article 5 was attracted, not only because there was a fixed place where the assessees carried on their business, but also because they were 'service permanent establishments' and 'agency permanent establishments' under article 5. In an appeal to the Income-tax Appellate Tribunal, the Income-tax Appellate Tribunal held that the Commissioner of Income (Appeals) was right in holding that a 'fixed place permanent establishment' and 'service permanent establishment' had been made out under article 5, but said nothing about the 'agency permanent establishment' as that was not argued by the Revenue before the Income-tax Appellate Tribunal. However, the Income-tax Appellate Tribunal, on a calculation formula different from that of the Commissioner of Income (Appeals), arrived at a nil figure of income for all the relevant assessment years.

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1. [2017] 399 ITR 34 (SC) ; [2018] 13 SCC 294.
2. Page 41 of 399 ITR.

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The appeal of the assessees to the High Court proved successful and the High Court, by an elaborate judgment, has set aside the findings of all the authorities referred to above, and further dismissed the cross-appeals of the Revenue. Consequently, the Revenue is before us in these appeals."

The court, after analysing the decisions and the concerned report produced before it, observed in paragraph 22 as follows[1] :

"*This report would show that no part of the main business and revenue earning activity of the two American companies is carried on through a fixed business place in India which has been put at their disposal. It is clear from the above that the Indian company only renders support services which enable the assessees in turn to render services to their clients abroad. This outsourcing of work to India would not give rise to a fixed place permanent establishment and the High Court judgment is, therefore, correct on this score.*" (emphasis[2] supplied)

We may usefully refer to paragraphs 24 and 26 of the reported decision, which read thus[3] :

"It has already been seen that none of the customers of the assessees are located in India or have received any services in India. This being the case, it is clear that the very first ingredient contained in article 5(2)(i) is not satisfied. However, the learned Attorney General, relying upon Para 42.31 of the OECD Commentary, has argued that services have to be furnished within India, which does not mean that they have to be furnished to customers in India. Para 42.31 of the OECD Commentary reads as under :

'42.31 . . . Whether or not the relevant services are furnished to a resident of a State does not matter : what matters is that the services are performed in the State through an individual present in that State . . .

We entirely agree with the approach of the High Court in this regard. Para 42.31 of the OECD Commentary does not mean that services need not be rendered by the foreign assessees in India. *If any customer is rendered a service in India, whether resident in India or outside India, a 'service permanent establishment' would be established in India.* As has been noticed by us hereinabove, no customer, resident or otherwise, receives any service in India from the assessees. All its customers receive services only in locations outside India. Only

1. Page 63 of 399 ITR.
2. Here printed in italics.
3. Page 65 of 399 ITR.

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auxiliary operations that facilitate such services are carried out in India. This being so, it is not necessary to advert to the other ground, namely, that 'other personnel' would cover personnel employed by the Indian company as well, and that the US companies through such personnel are furnishing services in India. This being the case, it is clear that as the very first part of article 5(2)(i) is not attracted, the question of going to any other part of the said article does not arise. It is perhaps for this reason that the Assessing Officer did not give any finding on this score." (emphasis[1] supplied)

As aforesaid, we agree with the finding recorded by the High Court about the nature and character of stated activities carried on by the liaison offices of the respondent and in our view, the High Court justly reckoned the same as being of preparatory or auxiliary character, falling under article 5(3)(e).

13 The High Court has also examined the matter in the context of *Explanation* to section 9(1)(i) of the 1961 Act. Prior to enactment of the Finance Act, 2003 (32 of 2003), section 9(1)(i) read thus :

"9. *Income deemed to accrue or arise in India*.—(1) The following incomes shall be deemed to accrue or arise in India—

(i) all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situate in India.

Explanation 1.— For the purposes of this clause—

(a) in the case of a business of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India ;

(b) in the case of a non-resident, no income shall be deemed to accrue or arise in India to him through or from operations which are confined to the purchase of goods in India for the purpose of export ;

(c) in the case of a non-resident, being a person engaged in the business of running a news agency or of publishing newspapers, magazines or journals, no income shall be deemed to accrue or arise in India to him through or from activities which are confined to the collection of news and views in India for transmission out of India ;

(d) in the case of a non-resident, being—

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(1) an individual who is not a citizen of India ; or

(2) a firm which does not have any partner who is a citizen of India or who is resident in India ; or

(3) a company which does not have any shareholder who is a citizen of India or who is resident in India,

no income shall be deemed to accrue or arise in India to such individual, firm or company through or from operations which are confined to the shooting of any cinematograph film in India . . ."

After the enactment of Finance Act, 2003, *Explanation 2* came to be inserted after the renumbered *Explanation 1* to clause (i) of sub-section (1) of section 9 with effect from April 1, 2004. The same reads thus :

"9. *Income deemed to accrue or arise in India*.—(1) The following incomes shall be deemed to accrue or arise in India—

(i) all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situate in India . . .

Explanation 2.—For the removal of doubts, it is hereby declared that 'business connection' shall include any business activity carried out through a person who, acting on behalf of the non-resident,—

(a) has and habitually exercises in India, an authority to conclude contracts on behalf of the non-resident, unless his activities are limited to the purchase of goods or merchandise for the non-resident ; or

(b) has no such authority, but habitually maintains in India a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the non-resident ; or

(c) habitually secures orders in India, mainly or wholly for the non-resident or that non-resident and other non-residents controlling, controlled by, or subject to the same common control, as that non-resident :

Provided that such business connection shall not include any business activity carried out through a broker, general commission agent or any other agent having an independent status, if such broker, general commission agent or any other agent having an independent status is acting in the ordinary course of his business :

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Provided further that where such broker, general commission agent or any other agent works mainly or wholly on behalf of a non-resident (hereafter in this proviso referred to as the principal non-resident) or on behalf of such non-resident and other non-residents which are controlled by the principal non-resident or have a controlling interest in the principle non-resident or are subject to the same common control as the principal non-resident, he shall not be deemed to be a broker, general commission agent or an agent of an independent status."

The meaning of expressions "business connection" and "business activity" has been articulated. However, even if the stated activity(ies) of the liaison office of the respondent in India is regarded as business activity, as noted earlier, the same being "of preparatory or auxiliary character" ; by virtue of article 5(3)(e) of the double taxation avoidance agreement, the fixed place of business (liaison office) of the respondent in India otherwise a permanent establishment, is deemed to be expressly excluded from being so. And since by a legal fiction it is deemed not to be a permanent establishment of the respondent in India, it is not amenable to tax liability in terms of article 7 of the double taxation avoidance agreement.

Taking any view of the matter, therefore, we find no substance in this appeal. We uphold the conclusions reached by the High Court for the reasons stated hitherto. **14**

Accordingly, the appeal is dismissed with no order as to costs. Pending interlocutory applications, if any, shall stand disposed of. **15**

[2020] 425 ITR 63 (Mad)

[IN THE MADRAS HIGH COURT]

TAMIL NADU LEATHER TANNERS EXPORTERS IMPORTERS ASSOCIATION

v.

DEPUTY DIRECTOR OF INCOME-TAX (EXEMPTIONS)

T. S. SIVAGNANAM and **MRS. V. BHAVANI SUBBAROYAN** JJ.

June 24, 2019.

SS ▸ ITA 1961, ss 2(15), 11, 12AA
AY ▸ 2009-10 to 2011-12
HF ▸ Remanded

CHARITABLE PURPOSE—EXEMPTION—ASSESSEE REGISTERED UNDER SECTION 12AA—DENIAL OF EXEMPTION ON GROUND THAT ACTIVITY OF

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IMPORT AND DISTRIBUTION OF RAW MATERIAL BY ASSESSEE AMOUNTED TO COMMERCIAL ACTIVITY—FACTUAL MATRIX TO BE EXAMINED IN GREATER DEPTH BY TRIBUNAL—MATTER REMANDED TO TRIBUNAL—INCOME-TAX ACT, 1961, ss. 2(15), 11, 12AA.

The assessee was a public charitable trust registered under section 12AA of the Income-tax Act, 1961 from the assessment year 1999-2000. The assessee imported and distributed wattle extracts (which constituted one of the cleaning agents for processing raw hides). For the assessment years 2009-10, 2010-11 and 2011-12, the Assessing Officer held that the wattle extract purchased by the assessee from abroad and sold it at a lower price which was not less than the cost of the goods and that the assessee earned profits out of such activity. The explanation given by the assessee that it was an activity of distribution was rejected by the Assessing Officer. He recommended for cancellation of the registration of the assessee and assessed the assessee as an association of persons. The Commissioner (Appeals) allowed the appeals filed by the assessee. The Tribunal held that the trading activities engaged in by the assessee were not mentioned in its objectives, that its activities of import of raw material from abroad and distribution of such raw material amounted to commercial transaction and a trading activity which generated profits and denied the exemption under section 11 to the assessee. On appeals :

Held, *that the denial of benefits of tax exemption under section 11 on the ground that the activities of import and distribution of wattle extracts was commercial in nature within the scope of the provisos to section 2(15) though the assessee was registered under section 12A(a) required reconsideration and examination in greater depth by the Tribunal. The findings of the Tribunal were insufficient to reverse the order of the Commissioner (Appeals). It was required to take note of the legal position which prevailed at the relevant time. The order passed by the Tribunal was set aside and the matter was to be remanded to it for fresh consideration. [Matter remanded.]*

Cases referred to :

CIT *v.* India Pepper and Spice Trade Association [1978] 111 ITR 206 (Ker) (para 11)

CIT (Addl.) *v.* South India Hire Purchase Association [1979] 116 ITR 793 (Mad) (para 11)

India Trade Promotion Organization *v.* DGIT (Exemptions) [2015] 371 ITR 333 (Delhi) (para 11)

Institute of Chartered Accountants of India *v.* DGIT (Exemptions) [2013] 358 ITR 91 (Delhi) (para 11)

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Madras Kirana Merchants Association *v.* CIT [1978] 111 ITR 156 (Mad) (para 11)

Tax Case Nos. 705 to 707 of 2018.

A. S. Sriraman for the appellant.

J. Narayanaswamy, Senior Standing Counsel, for the respondent.

JUDGMENT

The judgment of the court was delivered by

1 T. S. SIVAGNANAM J.—These tax case appeals by the assessee, filed under section 260A of the Income-tax Act, 1961, ("the Act" for brevity) are directed against the common order passed by the Income-tax Appellate Tribunal, Madras "B" Bench, Chennai in I. T. A Nos. 2006/Mds/2016, 2007/Mds/2016 and 2008/Mds/2016, dated August 3, 2017 for the assessment years 2009-10, 2010-11 and 2011-12, respectively.

2 The above tax case appeals have been filed raising the following substantial questions of law :

> "(i) Whether the Appellate Tribunal is correct in law in denying the tax exemption under section 11 of the Act for the assessment years under consideration despite the continued availability of registration under section 12A(a) of the Act for the appellant as a public charitable trust ?
>
> 2. Whether the Appellate Tribunal is correct in law in denying the tax exemption under section 11 of the Act for the assessment years under consideration on the misconstruction of the provisos below section 2(15) of the Act while recording perverse findings of fact on the activity pursued as a trading activity ?
>
> 3. Whether the Appellate Tribunal is correct in confirming the assessment orders passed for the assessment years under consideration without examining the objects and financial statements of the appellant for the purpose of considering the grant of tax exemption on the principles of mutuality ?"

3 We have heard Mr. A. S. Sriraman, learned counsel for the appellant and Mr. J. Narayanaswami, learned senior standing counsel for the respondent. On consent of either side, we take up the appeals for final disposal.

4 The assessment for the years under consideration was completed by the Assessing Officer vide orders dated December 28, 2011, February 4, 2013 and November 29, 2013, respectively. The Assessing Officer held that,

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there is no denying to the fact that wattle extract purchased from abroad was sold at a lower price which is not less than the cost of the goods. The explanation given by the assessee that this is an activity of distribution was rejected by the Assessing Officer and it was held that the assessee has earned profits out of the activity of selling wattle extract. Since the assessee enjoyed the benefit of exemption by virtue of registration under section 12AA of the Act, the Assessing Officer recommended for cancellation of the registration and proceeded to assess the appellant-assessee as an association of persons (AoP).

5 The assessee filed appeals before the Commissioner of Income-tax (Appeals)-VII (CIT(A)) raising various contentions and relying upon several decisions. The Commissioner of Income-tax (Appeals) by an order dated March 28, 2016 allowed the appeals.

6 The Revenue preferred appeals before the Tribunal contending that the assessee's activities are purely in the nature of trade, commerce or business thereby bringing their case squarely under the proviso to section 2(15) of the Act. The Tribunal in paragraph 6 of the impugned order extracted the findings of the Commissioner of Income-tax (Appeals). In paragraphs 7 and 8, the stand taken by the authorised representative of the assessee has been referred to. The discussion is in paragraph 9.

7 We find that the only finding recorded by the Tribunal is that from the objectives of the assessee-trust, it is evident that the trading activities indulged by them is not mentioned in the objectives of the society. Moreover, the activities of the assessee-society, namely, procuring raw material from abroad and distributing the same will amount to pure commercial transaction because it is purely a trading activity generating substantial profit.

8 In our considered view, this finding is insufficient to dislodge the order passed by the Commissioner of Income-tax (Appeals). We say so for more than one reason. Firstly, the Tribunal was required to take note of the legal position, which prevailed at the relevant time, in fact, one of the decisions of the Tribunal which considered similar case in respect of *Asst. CIT (Exemptions)* v. *All India Skin and Hide Tanners and Merchants Association* in I. T. A. No. 2749 to 2751/Mds/1994 dated March 25, 2013, was available when the Tribunal decided the impugned appeals. In the said decision, the Tribunal elaborately discussed the issue, examined the memorandum of association of the said assessee-association and held in favour of the assessee.

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9 Mr. J. Narayanaswami, learned senior standing counsel for the Revenue submitted that the decision has not been accepted by the Department and they have preferred an appeal. Be that as it may, what is required to be seen in the instant case is with regard to the objects of the association and as to whether their activity would fall within the scope of advancement of any other object of general public utility.

10 It was also necessary to consider the fact of Circular No. 11 of 2008 dated December 19, 2008 ([2009] 308 ITR (St.) 5), issued by the Central Board of Direct Taxes and the operative portion of which are as follows :

> "3.1. There are industry and trade associations who claim exemption from tax under section 11 on the ground that their objects are for charitable purpose as these are covered under 'any other object of general public utility'. Under the principle of mutuality, if trading takes place between persons who are associated together and contribute to a common fund for the financing of some venture or object and in this respect have no dealings or relations with any outside body, then any surplus returned to the persons forming such association is not chargeable to tax. In such cases, there must be complete identity between the contributors and the participants. Therefore, where industry or trade associations claim both to be charitable institutions as well as mutual organizations and their activities are restricted to contributions from and participation of only their members, these would not fall under the purview of the proviso to section 2(15) owing to the principle of mutuality. However, if such organizations have dealings with non-members, their claim to be charitable organisations would now be governed by the additional conditions stipulated in the proviso to section 2(15)."

11 Further, we may note the decisions on this point more particularly the following : *India Trade Promotion Organization* v. *DGIT (Exemptions)* [2015] 371 ITR 333 (Delhi) ; *Institute of Chartered Accountants of India* v. *DGIT (Exemptions)* [2013] 358 ITR 91 (Delhi) ; *Addl. CIT* v. *South India Hire Purchase Association* [1979] 116 ITR 793 (Mad) ; *CIT* v. *India Pepper and Spice Trade Association* [1978] 111 ITR 206 (Ker) and *Madras Kirana Merchants Association* v. *CIT* [1978] 111 ITR 156 (Mad).

12 Apart from the above decisions, there are other decisions of the Chennai Bench of the Tribunal in the case of *CIT (Exemptions)* v. *All India Skin and Hide Tanners and Merchants Association* in I. T. A. Nos. 1240 to 1242/Mds/2016 dated September 23, 2016 and *CIT (Exemptions)* v. *All India Skin and Hide Tanners and Merchants Association* in I. T. A. No. 1851/Mds/2017, dated October 6, 2017.

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13 In this case also the earlier decision of the Tribunal dated March 25, 2013 has been referred to. We have pointed out these orders only for the purpose that in those cases the objectives of the concerned assessee were analysed by the Tribunal. However, we find such exercise was not done in the instant case, which was required to be done. We also make it clear that we have not expressed any opinion on the merits of the matter but, what we are concerned is that, an exercise should be done to examine the contention advanced by the assessee. More particularly, the contention which were raised in this appeal and the decisions which were cited at the bar.

14 One more aspect which weighed in our minds is the show-cause notices issued by the Director of Income-tax (Exemptions). The first of which was issued on March 4, 2009, calling upon the assessee to explain as to why the registration granted under section 12AA of the Act should not be cancelled. The assessee submitted their reply dated March 27, 2009, no orders were passed and the matter was not pursued further. Subsequently, the Director of Income-tax (Exemptions) issued another show-cause notice on November 1, 2011 for the same purpose. The assessee submitted their reply dated November 16, 2011. In the said reply, the following stand was taken by the assessee :

> "(g) As explained above, our association have imported wattle extract, a raw material essential for leather tanning and available only in African countries and distributed among the members of the trade at a lesser rate than that usually available in the market. For the service the association has never charged any fee, cess or any other consideration from the individual receivers and users.
>
> (h) Instead of individual member placing order in the foreign countries, wasting time, labour and money in import formalities, the association pooled the demand and placed bulk orders resulting in large economy. Even this activity of the association is assumed to, but without conceding, in the nature of service rendering to any trade, commerce or business, but definitely not carried out for any cess or fee or any other consideration.
>
> (i) Proviso to section 2(15) of the Income-tax Act does not exclude the activity involved in the nature of trade, commerce or business or rendering any service in relation to any trade, commerce, or business in entirety from the definition of "charitable purpose", but it outlined the above referred to activities from the ambit of the definition of "charitable purpose" only if it is carried out for a cess or fee or any other consideration.

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(j) In our association's case, from the wattle extract distribution activity some surpluses are arising due to the following reasons :

(i) At the time of clearing the consignment of wattle extract from foreign countries, the exact cost per ton could not be ascertained because of interest rate and uncertainty in the period of repayment of loan availed of from the bank for importing the raw materials and fluctuations in foreign exchange.

(ii) So the association fixed an 'ad hoc' cost for distribution of wattle extract with the help of market experts in such a manner that the 'ad hoc' cost fixed should not exceed the price for the same material available in the market and at the same time it should not cost the association a loss.

Thus the wattle extract distribution and the cost fixing for the distribution are done neither with any profit motive nor for any cess, fee or other consideration.

(k) Thus wattle extract distribution activity carried out by the association is not done for any cess or fee or any other consideration and hence submit that the association does not violate the provisions contained in section 2(15) of the Income-tax Act.

(8) To sum up, the honourable Director of Income-tax (Exemptions) proposal to initiate proceeding under section 12AA(3) is wholly devoid of merits and is not based on any valid or proper provisions of law. The amendment to section 2(15) by itself does not vest in the Director of Income-tax (Exemptions) the power to cancel the registration of a trust which carries on, among others, certain objects constituting the 'advancement of general public utility'. Even where the fourth limb of the definition is included as part of the objects of the trust it is only that specified object which can be linked and treated as non-charitable and would not justify the cancellation of the registration of the trust as a whole.

In the above circumstances, we request the honourable Director of Income-tax (Exemptions) to drop his proposal to initiate proceedings under section 12AA(3)."

15 The learned counsel appearing for the appellant/assessee submitted that on receipt of the aforementioned reply the proceeding proposing to cancel the said registration under section 12AA was dropped and till date the assessee is enjoying such registration. However, Mr. J. Narayanaswami, learned senior standing counsel, does not have any instructions in that

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regard but would submit that in any event, the facts of the case is the only relevant factor to be gone into.

16 In the light of the above, we are of the opinion that the matter requires reconsideration by the Tribunal by examining the factual matrix in greater depth. For the above reason, this appeal is allowed. The order passed by the Tribunal is set aside and the matter is remanded back to the Tribunal for fresh consideration to consider all the issues that may be raised by the assessee as well as by the Revenue. We make it clear that we have not expressed any opinion on the merits of the contentions advanced by the appellant/assessee nor the defence, which was raised before this court by Mr. J. Narayanaswami learned counsel for the Revenue.

17 Consequently, the substantial questions of law are left open. No costs.

[2020] 425 ITR 70 (Guj)

[IN THE GUJARAT HIGH COURT]

PANKAJBHAI JAYSUKHLAL SHAH

(c/o. Meena Agency Ltd.)

v.

ASSISTANT COMMISSIONER OF INCOME-TAX AND ANOTHER

MS. HARSHA DEVANI and **BHARGAV D. KARIA** JJ.

April 9, 2019.

SS ▸ ITA 1961, ss 147, 148, 292B
AY ▸ 2011-12
HF ▸ Assessee

REASSESSMENT—NOTICE—VALIDITY—OFFICER RECORDING REASONS AND ISSUING NOTICE MUST BE THE JURISDICTIONAL ASSESSING OFFICER—REASONS RECORDED BY JURISDICTIONAL ASSESSING OFFICER BUT NOTICE ISSUED BY OFFICER WHO DID NOT HAVE JURISDICTION OVER ASSESSEE—DEFECT NOT CURABLE UNDER SECTION 292B—NOTICE AND CONSEQUENTIAL PROCEEDINGS AND ORDER INVALID—INCOME-TAX ACT, 1961, SS. 147, 148, 292B.

Since the notice under section 148 of the Income-tax Act, 1961, is a jurisdictional notice, any inherent defect therein cannot be cured under section 292B. A notice under section 148(1) would be a valid notice if the jurisdictional Assessing Officer records the reasons for reopening the assessment as

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contemplated under sub-section (2) of section 148 and thereafter the same Officer namely the jurisdictional Assessing Officer issues the notice under section 148(1).

For the assessment year 2011-12 an order under section 143(1) was passed against the assessee. Thereafter, a notice dated March 29, 2018 under section 148 was issued to reopen the assessment under section 147 in response to which, the assessee submitted that the original return filed by him be treated as the return filed in response to the notice under section 148 and requested the Assessing Officer to supply a copy of the reasons recorded for reopening the assessment. . The assessee participated in the assessment proceedings and raised objections against the initiation of proceedings under section 147 on the ground that the assumption of jurisdiction on the part of the Assessing Officer by issuance of notice under section 148 was invalid contending that the notice was issued by the Income-tax Officer, Ward No. 2(2), whereas the reasons were recorded by the Deputy Commissioner of Income-tax, Circle 2. The Department contended that issuance of the notice by the Income-tax Officer was a procedural lapse which had happened on account of the mandate of e-assessment scheme and non-migration of the permanent account number of the assessee in time and that such defect was covered under the provisions of section 292B and therefore, the notice issued could not be said to be invalid. On a writ petition :

Held, *allowing the petition, that while the reasons for reopening the assessment had been recorded by the jurisdictional Assessing Officer, viz., the Deputy Commissioner, Circle 2, the notice under section 148(1) had been issued by the Income-tax Officer, Ward 2(2), who had no jurisdiction over the assessee, and hence, such a notice was bad on the count of having been issued by an Officer who had no authority to issue such notice. It was the Officer recording the reasons who had to issue the notice under section 148(1) whereas the reasons had been recorded by the jurisdictional Assessing Officer and the notice had been issued by an Officer who did not have jurisdiction over the assessee. The notice under section 148 being a jurisdictional notice, any inherent defect therein could not be cured under section 292B. It was not possible for the jurisdictional Assessing Officer, viz., the Deputy Commissioner to issue the notice under section 148 on or before March 31, 2018 as migration of the permanent account number was not possible within that short period and therefore, the Income-tax Officer had issued the notice instead of the jurisdictional Assessing Officer. Thus there was an admission on the part of the Department that the Deputy Commissioner, Circle 2, who had jurisdiction over the assessee had not issued the notice under section 148 but it*

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was the Income-tax Officer, Ward 2(2) who did not have any jurisdiction over the assessee who had issued such notice. No proceedings could have been taken under section 147 in pursuance of such invalid notice. The notice under section 148(1) and all the proceedings taken pursuant thereto could not be sustained.

HYNOUP FOOD AND OIL INDUSTRIES LTD. *v.* ASST. CIT [2008] 307 ITR 115 (Guj) *followed*.

[The Supreme Court has dismissed special leave petition filed by the Department against this judgment.—Ed.]

HYNOUP FOOD AND OIL INDUSTRIES LTD. *v.* ASST. CIT [2008] 307 ITR 115 (Guj) (para 5) *referred to.*

R/Special Civil Application No. 230 of 2019.

Darshan B. Gandhi and *S. P. Majmudar* for the petitioner.

Mrs. Mauna M. Bhatt for the respondents.

JUDGMENT[1]

The judgment of the court was delivered by

1 MS. HARSHA DEVANI J.—Rule. Mrs. Mauna Bhatt, learned senior standing counsel waives service of notice of rule on behalf of the respondents.

2 Having regard to the controversy involved in the present case, which lies in a narrow compass and with the consent of the learned advocates for the respective parties, the matter was taken up for final hearing today.

3 By this petition under article 226 of the Constitution of India, the petitioner has challenged the notice dated March 29, 2018 issued by the Income-tax Officer, Ward 2(2), Jamnagar under section 148 of the Income-tax Act, 1961 (hereinafter referred to as the "Act") seeking to reopen the assessment of the petitioner for the assessment year 2011-12. It appears that before this petition came to be filed, the Assessing Officer has proceeded further pursuant to the impugned notice and has passed the assessment order. However, since the issue raised in the present petition is a jurisdictional issue, this court had issued notice in the matter.

4 The facts stated briefly are that, the petitioner herein filed return of income for the assessment year 2011-12 on September 1, 2012 declaring total income of Rs. 44,05,746. The return was processed under section 143(1) of the Act. Thereafter, by the impugned notice dated March 29, 2018, the Income-tax Officer, Ward 2(2), Jamnagar, sought to reopen the assessment of the petitioner for the assessment year 2011-12. In response to the notice, the petitioner submitted that the return filed by him on

1. Oral judgment.

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August 31, 2012 be treated as the return filed in response to the notice under section 148 of the Act and requested the Assessing Officer to supply a copy of the reasons recorded for reopening the assessment.

(4.1) It appears that after the issuance of the notice under section 148 of the Act, the charge over the petitioner's case was transferred to the Assistant Commissioner of Income-tax (Asst. CIT) who is the current Assessing Officer of the petitioner.

(4.2) Upon receipt of the reasons recorded, the petitioner found that the same had been recorded by the Deputy Commissioner of Income-tax (Deputy CIT), Circle-2, Jamnagar. It appears that in the meanwhile, the petitioner participated in the assessment proceedings. Thereafter, by a letter dated December 20, 2018, the petitioner raised objections against the initiation of proceedings under section 147 of the Act. Before such objections could be decided by the respondent, the petitioner has filed the present petition seeking reliefs noted hereinabove.

5 Mr. Darshan Gandhi, learned advocate for the petitioner invited the attention of the court to the impugned notice to point out that the same has been issued by one Mr. Neeraj Kumar, Income-tax Officer, Ward 2(2), Jamnagar. Referring to the reasons recorded, it was pointed out that the same has been recorded by one Mr. Chintamani V. Dingankar, Deputy Commissioner of Income-tax, Circle-2, Jamnagar. Reference was made to section 148 of the Act, which provides for issue of notice where income has escaped assessment and, more particularly, to sub-section (2) thereof, which provides that the Assessing Officer shall, before issuing any notice under this section, record his reasons for doing so. It was submitted that the notice under section 148 of the Act is required to be issued by the Assessing Officer who recorded the reasons; whereas in the facts of the present case, the reasons have been recorded by the Deputy Commissioner of Income-tax whereas the impugned notice has been issued by the Income-tax Officer and hence, the notice under section 148 of the Act is without jurisdiction. In support of his submission, learned advocate for the petitioner has placed reliance upon the decision of this court in the case of *Hynoup Food and Oil Industries Ltd.* v. *Asst. CIT* [2008] 307 ITR 115 (Guj), wherein the court after referring to the provisions of sections 147 and 148 of the Act, held that when section 147 is read in conjunction with section 148(2) of the Act which mandates that the Assessing Officer shall, before issuing any notice under section 148(1) of the Act, record his reasons for issuing the notice, it is clear that the Officer recording the reasons under section 148(2) and the Officer issuing the notice under section 148(1) has to be the same person. The court further observed that the form of the

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notice itself indicates that the authority has to record "whereas I have reason to believe that income liable to tax for the assessment year has escaped assessment within the meaning of section 147 of the Income-tax Act, 1961". Accordingly, the court held that the notice which was issued by an Officer other than the Officer who had recorded the reasons was invalid. Mr. Gandhi submitted that the above decision would be squarely applicable to the facts of the present case and hence, the impugned notice which is a jurisdictional notice is invalid and without authority of law. It was, accordingly, urged that the petition deserves to be allowed by setting aside the impugned notice.

6 Opposing the petition, Mrs. Mauna Bhatt, learned senior standing counsel for the respondents, submitted that in this case the petitioner has responded to the notice issued under section 148 of the Act and has participated in the proceedings pursuant thereto, which have culminated into the impugned assessment order. It was submitted that the petitioner is, therefore, required to be relegated to the remedy of appeal under the relevant statutory provisions. It was further submitted that the petitioner has initially participated in the proceedings under section 147 of the Act and has belatedly raised the objections and before such objections could be dealt with, has approached this court, and hence, this court may not entertain this petition at this stage.

(6.1) As regards the contention raised by the petitioner that the notice under section 148 of the Act having been issued by an Officer other than the Officer who recorded the reasons for reopening the assessment, the attention of the court was invited to the averments made in the affidavit-in-reply filed by the first respondent. It was submitted that the Assessing Officer, namely, Deputy Commissioner of Income-tax/Asst. Commissioner of Income-tax, Circle 2, Jamnagar who was holding the jurisdiction over the case recorded the reasons on March 27, 2018. Thereafter, as per the requirement of the Income-tax Act, 1961, the approval of the Principal Commissioner of Income-tax, Jamnagar was sought to issue the notice under section 148 of the Act on March 27, 2018. After such approval was given on March 28, 2018, the notice under section 148 of the Act was issued on March 29, 2018. For the purpose of explaining as to why the notice was issued by the Income-tax Officer and not the Deputy Commissioner of Income-tax who recorded the reasons, reference was made to the averments made in paragraph 4 of the above affidavit-in-reply reference to which shall be made hereinafter. It was submitted that issuance of the notice by the Income-tax Officer is a procedural lapse which has happened on account of the mandate of e-assessment scheme and non-migration of

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permanent account number in time. It was submitted that this being a procedural lapse, such defect would be covered under the provisions of section 292B of the Act and therefore, the impugned notice cannot be said to be invalid. It was submitted that the petitioner having participated in the reassessment proceedings, pursuant to which the reassessment order came to be passed on December 28, 2018, it is not permissible for the petitioner to now challenge the impugned notice on the ground of invalidity, in view of the provisions of section 292B of the Act. It was, accordingly, urged that the petition being devoid of merits, deserves to be dismissed.

7 Having regard to the conduct of the petitioner of participating in the proceedings before the Assessing Officer and thereafter, at the later stage, filing objections and approaching this court before such objections could be disposed of, ordinarily this court would be reluctant to interfere in such a case, more so, when the assessment order has already been passed, but having regard to the peculiar facts of the case, where the very jurisdiction of the Assessing Officer who issued the notice under section 148 of the Act is under challenge, this court has entertained the petition.

8 In the present case, what is the subject matter of challenge is the notice issued under section 148 of the Act on the ground that the assumption of jurisdiction on the part of the Assessing Officer by issuance of such notice is invalid. The sole contention on the basis of which such notice is challenged before this court is that the notice has been issued by the Income-tax Officer, Ward No. 2(2), Jamnagar, whereas the reasons have been recorded by the Deputy Commissioner of Income-tax, Circle 2, Jamnagar. In this regard, reference may be made to section 147 of the Act which provides that if the Assessing Officer has reason to believe that any income chargeable to tax has escaped assessment for any assessment year, he may, subject to the provisions of sections 148 to 153, assess or reassess such income and also any other income chargeable to tax which has escaped assessment and which comes to his notice subsequently during the course of the proceedings under that section. Section 148 of the Act provides for issue of notice where income has escaped assessment and provides that before making the assessment, reassessment or recomputation under section 147 of the Act, the Assessing Officer shall serve on the assessee a notice requiring him to furnish return of income as specified thereunder. Sub-section (2) thereof postulates that the Assessing Officer shall, before issuing any notice under that section, record his reasons for doing so.

9 This court in *Hynoup Food and Oil Industries Ltd.* (supra), has on a conjoint reading of sections 147 and 148(2) of the Act, held that the Officer recording the reasons under section 148(2) of the Act and the Officer

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issuing notice under section 148(1) of the Act has to be the same person. In this case, admittedly the Officer who recorded the reasons for reopening the assessment has not issued the notice under section 148(1) of the Act. In this regard, in response to the averments made in the petition regarding lack of jurisdiction on the part of the Assessing Officer on the ground of the impugned notice having been issued by an Officer other than the Officer who recorded the reasons, the first respondent has filed an affidavit-in-reply, wherein it has been averred thus :

> "3. . . . So the Assessing Officer, viz., the Deputy Commissioner of Income-tax/Assistant Commissioner of Income-tax, Circle 2, Jamnagar who was holding the jurisdiction over the case recorded the reasons on March 27, 2018. Thereafter, as per the requirement of the Income-tax Act, 1961, the approval of the Principal Commissioner of Income-tax, Jamnagar was sought to issue notice under section 148 on March 27, 2018. The Principal Commissioner of Income-tax, Jamnagar gave the approval to issue the notice under section 148 on March 28, 2018. Subsequently, the notice under section 148 was issued on March 29, 2018 . . .
>
> 4. . . . I submit that the reasons are recorded by Mr. Chintamani V. Dingankar, Deputy Commissioner of Income-tax, Circle 2, Jamnagar having jurisdiction over the petitioner. I submit that at the relevant point of time, the permanent account number of the petitioner was lying with the Income-tax Officer, Ward 2(2), Jamnagar as he was holding the territorial jurisdiction over the case and therefore, the impugned notice came to be issued by the Income-tax Officer, Ward 2(2) as the permanent account number could not be migrated at the last moment to the Deputy Commissioner of Income-tax, Circle 2. But as the income of the assessee was more than Rs. 15 lakhs, the Deputy Commissioner of Income-tax/Asst. Commissioner of Income-tax, Circle-2, Jamnagar held the jurisdiction over the case as per the Central Board of Direct Taxes instruction. The notice under section 148 was required to be issued by March 31, 2018 and the migration of the permanent account number was not possible in that short period. It is pertinent to mention that as per the prevailing scheme of e-assessment, the assessment was required to be made as e-assessment and all the correspondences/notices needed to be done online through the ITBA application as such correspondences/notices then goes to the e-filing account of the assessee which enables the assessee to respond through his/her e-filing account. As the permanent account number was lying in the jurisdiction of the Income-tax Officer, Ward

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2(2) Jamnagar, the notice was issued from the petitioner's Assessing Officer code. However, the assessment was completed by the Deputy Commissioner of Income-tax/Asst. Commissioner of Income-tax, Circle 2, Jamnagar who was holding the jurisdiction over the case and who recorded the reasons for reopening and formed his belief for reopening under section 147. Since the assessment was completed by the same Assessing Officer who recorded the reasons for reopening and who was holding the jurisdiction over the case, the validity of the issued notice is correct and it is not a case of borrowed opinion. It was a procedural lapse which was (sic. had) happened on account of mandate of e-assessment scheme and non-migration of permanent account number in time."

From the averments made in the affidavit-in-reply filed on behalf of the respondent, it is evident that it was the Deputy Commissioner of Income-tax, Circle 2, Jamnagar, who had jurisdiction over the petitioner. Previously the Income-tax Officer, Ward 2(2), Jamnagar was having jurisdiction over the petitioner, however, as per the Central Board of Direct Taxes instructions, in view of the fact that the income of the assessee was more than Rs. 15 lakhs, the Deputy Commissioner of Income-tax/Asst. Commissioner of Income-tax, Jamnagar held the jurisdiction over the petitioner. It appears that it was not possible for the jurisdictional Assessing Officer, viz., the Deputy Commissioner of Income-tax to issue the notice under section 148 of the Act on or before March 31, 2018 as migration of the permanent account number was not possible within that short period. Therefore, the Income-tax Officer has issued the notice under section 148 of the Act instead of the jurisdictional Assessing Officer. Thus there is an admission on the part of the first respondent that the Deputy Commissioner of Income-tax, Circle 2, Jamnagar who had the jurisdiction over the petitioner had not issued the notice under section 148 of the Act but it is the Income-tax Officer, Ward 2(2), Jamnagar, who did not have any jurisdiction over the petitioner, in respect of the present case, who had issued such notice. As held by this court in the case of *Hynoup Food and Oil Industries Ltd.* (supra), it is the Officer who records the reasons who has to issue the notice under section 148(1) of the Act whereas in the present case the reasons have been recorded by the jurisdictional Assessing Officer, whereas the notice under section 148(1) of the Act has been issued by an Officer who did not have jurisdiction over the petitioner. Since the notice under section 148 of the Act is a jurisdictional notice, any inherent defect therein cannot be cured under section 292B of the Act. A notice under section 148(1) of the Act would be a valid notice if the jurisdictional Assessing

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Officer records the reasons for reopening the assessment as contemplated under sub-section (2) of section 148 and thereafter the same Officer namely the jurisdictional Assessing Officer issues the notice under section 148(1) of the Act. In the facts of the present case, while the reasons for reopening the assessment have been recorded by the jurisdictional Assessing Officer, viz., the Deputy Commissioner of Income-tax, Circle 2, Jamnagar, the impugned notice under section 148(1) of the Act has been issued by the Income-tax Officer, Ward 2(2), Jamnagar who had no jurisdiction over the petitioner, and hence, such a notice was bad on the count of having been issued by an Officer who had no authority in law to issue such notice. As a necessary corollary it follows that no proceedings could have been taken under section 147 of the Act in pursuance of such invalid notice. In the aforesaid premises, the impugned notice under section 148(1) of the Act as well as all the proceedings taken pursuant thereto cannot be sustained.

11 It may be noted that before the Assessing Officer, during the course of the assessment proceedings also, the petitioner had raised such objections with regard to the jurisdiction of the Assessing Officer. However, the Assessing Officer has proceeded further and instead of recording the objections raised by the petitioner, namely that the notice has been issued by the Income-tax Officer though the reasons have been recorded by the Deputy Commissioner of Income-tax, has recorded that the notice was issued by the Deputy Commissioner of Income-tax, Circle 2 and subsequently, Asst. Commissioner of Income-tax was holding charge of Circle 2 and, therefore, there was no harm in passing the assessment order. It, therefore, appears that the Assessing Officer has not even understood the contention raised by the petitioner during the course of the assessment proceedings.

12 In the light of the above discussion, the petition succeeds and is accordingly allowed. The impugned notice dated March 29, 2018 issued under section 148 of the Income-tax Act, 1961, and all the proceedings pursuant thereto including the assessment order dated December 28, 2018 are hereby quashed and set aside.

13 Rule is made absolute accordingly with no order as to costs.

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[2020] 425 ITR 79 (Guj)

[IN THE GUJARAT HIGH COURT]

ARUN MUNSHAW HUF

v.

INCOME-TAX OFFICER

J. B. PARDIWALA and **BHARGAV D. KARIA** JJ.

January 13, 2020.

SS ▸ ITA 1961, ss 147, 148
AY ▸ 1991-92
HF ▸ Assessee

REASSESSMENT—NOTICE AFTER FOUR YEARS—VALIDITY—FAILURE TO DISCLOSE MATERIAL FACTS NECESSARY FOR ASSESSMENT—NO EVIDENCE OF SUCH FAILURE—NOTICE NOT VALID—INCOME-TAX ACT, 1961, ss. 147, 148.

Held, *that there was no tangible material with the Assessing Officer for the purpose of reopening the assessment except the change of opinion that the deductions could not have been claimed and allowed under sections 53(b) and 54(1)(i) of the Income-tax Act, 1961. The conveyance deed, permission of the appropriate authority to sell the property and other documents were filed by the assessee at the time of original assessment proceedings. Nothing was suppressed. Form 37-I speaks for itself. It was not in dispute that the notice under section 148 came to be issued beyond the period of four years. The Commissioner (Appeals) recorded a finding of fact that there was no failure on the part of the assessee to disclose fully and truly all the material facts necessary for the assessment. Such finding of fact could not have been disturbed by the Appellate Tribunal without any basis. The notice of reassessment was not valid.*

Cases referred to :

Calcutta Discount Co. Ltd. *v.* ITO [1961] 41 ITR 191 (SC) (para 3)

CIT *v.* Kelvinator of India Ltd. [2010] 320 ITR 561 (SC) (para 14)

CWT *v.* Azizunnisa Begum (Smt.) [2000] 243 ITR 852 (SC) (para 3)

Garden Silk Mills Ltd. *v.* Deputy CIT (Assessment) (No. 1) [1996] 222 ITR 27 (Guj) (para 2)

Hajee Mohamed Ibrahim *v.* GTO [1983] 143 ITR 333 (Karn) (para 3)

Nilamben Sandipbhai Parikh *v.* Asst. CIT [2019] 14 ITR-OL 587 (Guj) (para 14)

Omar Salay Mohamed Sait *v.* CIT [1959] 37 ITR 151 (SC) (para 16)

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Praful Chunilal Patel *v.* M. J. Makwana, Asst. CIT [1999] 236 ITR 832 (Guj) (para 2)

Rajesh Jhaveri Stock Brokers (P.) Ltd. *v.* Asst. CIT [2006] 284 ITR 593 (Guj) (para 13)

R/Tax Appeal No. 1091 of 2008.

Mrs. Swati Soparkar with *B. S. Soparkar* for the appellant.

Mrs. Mauna M. Bhatt for the respondent.

JUDGMENT[1]

The judgment of the court was delivered by

1 J. B. PARDIWALA J.—This tax appeal under section 260A of the Income-tax Act, 1961 (for short, "the Act 1961") is at the instance of an assessee and is directed against the order dated March 9, 2007 passed by the Income-tax Appellate Tribunal, Ahmedabad Bench "D" in I. T. A. No. 1113/Ahd/2001 for the assessment year 1991-92.

2 The facts giving rise to this appeal may be summarised as under :

The assessment was completed under section 143(3) of the Act, 1961 on March 28, 1994 on the total income of Rs. 75,404, which included the long-term capital gains of Rs. 61,812. The assessee sold a property being an agricultural land admeasuring 7,986 sq. yards in the form of a farmhouse along with water tank, servant quarter, etc., constructed on it for a consideration of Rs. 30,00,000 during the accounting year relevant to the assessment year 1991-92. The assessee claimed deduction under sections 53(b), 54(1)(i) and 54E of the Act, 1961 (as amended by the Finance Act, 1992) from the capital gains arising from the sale of the property. The deductions as claimed were allowed. The claim of the assessee was that the sale was of a residential house along with the land appurtenant thereto. Later, it was noticed by the Assessing Officer that the property in question was agricultural land and, therefore, the deduction under sections 53(b) and 54(1)(i) of the Act had been wrongly allowed. In such circumstances, the Assessing Officer reopened the assessment by issuing a notice under section 148 of the Act. The reassessment was accordingly completed withdrawing the deductions under sections 53(b) and 54(1)(i), respectively, of the Act. The long-term capital gains was determined at Rs. 17,11,363.

The assessee, being dissatisfied with the assessment order, preferred an appeal before the Commissioner of Income-tax (Appeals) VIII, Ahmedabad. The appeal preferred by the assessee came to be allowed by the Commissioner of Income-tax (Appeals) vide order dated March 13,

1. Oral judgment.

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2001. While allowing the appeal, the Commissioner of Income-tax (Appeals) held as under :

> "4. During the course of hearing of appeal, which was attended both by the authorised representative of the appellant and the present Assessing Officer, a report dated January 15, 2000 was sent by the Assessing Officer. In the said report, it was submitted that the Department's view with regard to the property sold by the appellant is that it was agricultural land and not residential property. The Assessing Officer has stated that in the deed of conveyance submitted at the time of assessment proceedings the property has been shown as agricultural land along with farm house and servant quarters, etc. and nothing has been mentioned about the nature of the construction or the area under construction described as farm house. It is also stated that during the course of assessment proceedings the assessee had not furnished any evidence whereby it could be held that the property in question was residential property and the same was actually used for the purpose. The Assessing Officer has further submitted that the wealth-tax return of the appellant for the assessment year 1990-91 shows that a bungalow mentioned as 'Avanti' has been disclosed in the statement of net wealth and at present also the assessee is staying in that bungalow, i.e., 'Avanti'. The Assessing Officer has, therefore, opined that the property declared in the conveyance deed as farm house was not the bungalow which was mentioned in the wealth-tax return for the assessment year 1990-91. Accordingly, the Assessing Officer was of the view that there was failure on the part of the assessee to disclose fully and truly all material facts necessary for assessment. The Assessing Officer has further submitted that though in the reasons recorded for the issue of notice under section 148 specific words regarding 'failure on the part of the assessee to disclose fully and truly all material facts necessary for assessment' have not been mentioned, his action was only as a result of the same. The Assessing Officer has also referred to the judgment of the hon'ble Gujarat High Court in the case of *Praful Chunilal Patel* v. *M. J. Makwana, Asst. CIT* [1999] 236 ITR 832 (Guj) for justifying the reopening of assessment in this case.
>
> 4.1 In view of the above report of the Assessing Officer, the Assessing Officer was again asked to be present for the hearing on February 15, 2001 wherein the issue pertaining to the reopening of assessment in this case was discussed with him and with the authorised representative of the appellant. In view of various doubts

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expressed by the Assessing Officer regarding the failure on the part of the assessee to disclose fully and truly all material facts during the original assessment proceedings, the Assessing Officer was required to make further inquiry with the appellant as to whether it was 'Avanti' bungalow which was sold or whether it was some other farm house on agricultural land which was the property in question. It was clarified by the appellant that the bungalow sold by the assessee was named as 'Avanti' and was situated at block No. 518. It is also stated that reference to bungalow situated at block No. 518 is made at various places in the deed of conveyance. It is also stated that in Form No. 37-I, there is a specific reference to a farm house along with water tank, servant quarter, etc. against the column – 'description and location of the property'. It is further clarified that on page No. 16 of the conveyance deed, it is specifically stated that there is block No. 512 situated on the eastern side of block No. 518. The assessee has also clarified that he had constructed a new bungalow on block No. 512, which has also been named as 'Avanti' by him and the assessee is presently living in that bungalow. The above clarifications of the assessee were forwarded to me by the Assessing Officer vide letter dated March 7, 2001. The Assessing Officer has, however, not refuted these clarifications.

5. I have considered the facts of the case and the contentions of the appellant and also heard the Assessing Officer in the matter. I have also considered the reports of the Assessing Officer dated January 15, 2001 and March 7, 2001. The reasons recorded by the Assessing Officer for reopening the assessment under section 147 of the Income-tax Act have also been gone through. The reasons show that on scrutiny of record the Assessing Officer noticed that during the year under consideration the assessee had sold agricultural land along with farm house built on it and deductions under sections 53(b), 54(1)(i) and 54E had been claimed from the capital gains. The Assessing Officer has further noticed that deductions under sections 53(b) and 54(1)(i) were not applicable to the assessee as these relate to residential property.

The above reasons show that the assessment was reopened because of the belief of the Assessing Officer that certain statutory deductions had been wrongly claimed and allowed. The reasons, however, do not indicate that the assessment was reopened on account of any material fact relating to the claim, which was not before the Assessing Officer at the time of original assessment and

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which came to the notice of the Assessing Officer subsequently. As far as the submissions made by the present Assessing Officer during the course of hearing of appeal are concerned, it is seen that the inquiry conducted on various points with the appellant shows that what was sold was an agricultural land having a farm house built on it, which was named by the assessee as 'Avanti'. The comparison of the information furnished during the original assessment proceedings with that of the wealth-tax records of the assessee (statement of net wealth for the assessment year 1990-91) does not show that the assessee had any other residential house besides this farm house built on agricultural land. Thus, what was required to be considered was, whether the farm house could be treated as bungalow more specifically as a residential house for the purposes of deduction under sections 53(b) and 54(1)(i) of the Income-tax Act or not. The facts do not, however, reveal that the appellant had himself misinformed the Department or failed to disclose any of the material facts. Even if a view is subsequently taken that the property sold was agricultural land and not a residential house with the land appurtenant thereto, it could only be inferred that a wrong claim for deduction was made but, it cannot be said that there was a failure on the part of the assessee to disclose all material facts relevant to the assessment. The relevant documents, i.e., conveyance deed ; permission of the appropriate authority giving the nature of the property sold, had been filed by the appellant at the time of original assessment proceedings. No new information or document came to the notice of the Assessing Officer so as to now hold that the deductions had been wrongly allowed, because the property sold was agricultural land and not residential house. It was only a change of opinion on the basis of the same factual information that the property in question was to be considered as agricultural land and not residential house for the purposes of capital gains. There was however, no failure on the part of the appellant to disclose fully and truly all material facts necessary for assessment.

5.1 In the case of *Garden Silk Mills Ltd.* v. *Deputy CIT (Assessment) (No. 1)* [1996] 222 ITR 27 (Guj), which was before the hon'ble Gujarat High Court, the assessee had claimed depreciation on increase in cost of machinery due to fluctuation in the rate of foreign exchange. Depreciation was allowed by the Income-tax Officer after considering the matter and allowance was also upheld on revision by the Commissioner of Income-tax. The reassessment proceedings

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were however initiated after 4 years on the ground that excessive depreciation had been allowed. It was held by the hon'ble High Court that the Assessing Officer was aware about the investment and fluctuations in the exchange rate and there was no failure on the part of the assessee to disclose any material facts necessary for assessment. The notice of reassessment was not valid and was required to be quashed.

5.3 The Assessing Officer in his report dated January 15, 2000 has relied on the judgment of the hon'ble Gujarat High Court in the case of *Praful Chunilal Patel* v. *M. J. Makwana, Asst. CIT* [1999] 236 ITR 832 (Guj). A perusal of the judgment shows that the power to make an assessment or reassessment within four years from the end of the relevant assessment year has been upheld by the hon'ble Gujarat High Court even in a case where there has been a complete disclosure of all relevant facts upon which a correct assessment might have been passed in the first instance irrespective of whether it is an error of fact or law that has been discovered or found out justifying the belief required to initiate the re-assessment proceedings. This judgment is not applicable in the case of the appellant as reassessment proceedings in this case have been initiated beyond four years from the end of the relevant assessment year.

6. Undisputedly the notice under section 148 has been issued beyond the period of 4 years from the end of the assessment year ended on March 31, 1992 as the notice under section 148 has been issued on January 22, 1998. Also as discussed in the preceding paras, there is no failure on the part of the assessee to disclose fully and truly all material facts necessary for assessment. The mistake, if any, committed by the Assessing Officer, is on account of improper appreciation of facts before him. Accordingly, the notice issued under section 148 is not a valid notice and any assessment framed in pursuance thereof is also not a valid assessment and is required to be annulled. The appellant succeeds on this point."

3 The Revenue, being dissatisfied with the order passed by the Commissioner of Income-tax (Appeals), went in appeal before the Income-tax Appellate Tribunal. The Appellate Tribunal, vide order dated March 9, 2007, allowed the appeal of the Revenue, thereby quashing and setting aside the order passed by the Commissioner of Income-tax (Appeals). We may quote the relevant part of the order passed by the Appellate Tribunal thus :

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"5.1 The reopening in the present case is clearly after the expiry of four years from the end of the relevant assessment year, so that the same could only be, in terms of the relevant section 147, where the assessee has failed to make a full and true disclosure of all material facts necessary for his assessment for the relevant year. In this regard, the scope and ambit of the words 'full and true' have to be properly appreciated, even as emphasised by the apex court in the case of *Calcutta Discount Co. Ltd.* v. *ITO* [1961] 41 ITR 191 (SC). Further, due regard has also to be given to *Explanation 1* to section 147 of the Act, which reads as :

'*Explanation 1.*—Production before the Assessing Officer of account books or other evidence from which material evidence could with due diligence have been discovered by the Assessing Officer will not necessarily amount to disclosure within the meaning of the foregoing proviso.'

5.2 If, therefore, as per the disclosure by the assessee, it can be said that he has disclosed all material facts necessary for his assessment for the relevant year, fully and truly, escapement of income, even if so, would only be attributable to the Assessing Officer, and for which the law protects the assessee by placing a cap of four years from the end of relevant assessment. The issue under reference is thus one of fact, to be decided in consideration of the material on record at the time of the original assessment, in which the assessee claimed and stood allowed the impugned deductions. In the present case, the assessee has not stated, as is apparent, in his return of income (copy of which is not placed on record, in spite of being specifically called for from the assessee at the time of hearing) :

(a) that what was sold stood described invariably as an agricultural land in the relevant conveyance deed, the primary document transferring the title to the capital asset under transfer ;

(b) the total area of the land subject to conveyance, including the area on which the residential house stood constructed ;

(c) the manner in which the sale rate of the property stood arrived at, i.e., whether as per the rates applicable to the agricultural land, or as a private land forming part of a residential house, and which stood separately valued (as the entire sale consideration, and thus, capital gains, stood considered as in respect of the residential property only) ;

(d) whether, the house, or a part of it was used as a farm house, i.e., for the beneficial user of the said land for agricultural purposes ; and

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(e) whether the dominant user of the house property was for residential purpose.

Further, he has also not explained the basis on which he considered the capital asset under transfer as a residential house and not an agricultural land, i.e., in whole or in part, in spite of agricultural operations being carried thereon, and further, being so stated in the conveyance deed itself, as well as the permission sought by the assessee from the appropriate authority (AA) for selling the same, by treating the said land only as appurtenant to the residential building situate thereon, entitling him, thus, to claim of deduction under sections 53(b) and 54(1)(i) of the Act with respect to the total amount of capital gains realised on the transfer of the capital asset.

5.3 There is no discussion in the assessment order of the nature of the capital gains, or of the deductions claimed thereagainst, and which would necessarily be the case had there been a disclosure on any one or more of the foregoing aspects of the transaction, all of which are unarguably material for the proper assessment of income under the said head (of income) for the relevant year. No doubt, as explained by the hon'ble jurisdictional High Court, the assessee's obligation is restricted to the disclosure of the primary facts only, with the inferential facts being left to the discretion of the Assessing Officer. Each of the aforesaid fact is a primary fact in relation to the assessment of the income arising on the aforesaid fact is a primary fact in relation to the assessment of the income arising on the transfer of the capital asset under question, lead as it does, to the determination of its nature as also the deductions exigible thereagainst. There is no expression of opinion in the original assessment order in the matter, for one to hold that the reason to believe of the escapement of income as being on account of a change of opinion, as stated by the learned Commissioner of Income-tax (Appeals). As such, we are of the firm view that the assessee has failed to make a full and true disclosure of all the material facts, necessary for his assessment, which he is obliged to in order to debar the initiation of reassessment proceedings in relation to the impugned assessment.

5.4 In fact, the arguments led by the assessee while contesting the reopening of his assessment, i.e., of having not sold a farm house, and of the same being described in his wealth-tax return as a residential house, were necessitated only by the fact of the aforesaid non-disclosure of the basic facts in relation to the impugned asset and its user, and which were necessary to arrive at a proper decision in the

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matter. Further, as would be apparent, the assessee has also cited thereat the decisions in the case of *Hajee Mohamed Ibrahim* v. *GTO* [1983] 143 ITR 333 (Karn) and *CWT* v. *Smt. Azizunnisa Begum* [2000] 243 ITR 852 (SC), contending their applicability to the facts of the present case. However, what is lost sight of, irrespective of the merits of the assessee's claim of the applicability of those decisions, is that the disclosure of facts as made, besides being inconsistent with the primary record, i.e., the conveyance deed, land revenue record, permission from the appropriate authority, was not sufficient or adequate to be able to apply the ratio of those decisions to the same. And which, on merits, rather, appear to be supportive of the Revenue's case, though by stating as much, we may clarify, that this may not be construed as an expression of opinion in the matter.

5.5 The learned Commissioner of Income-tax (Appeals) has directed investigation by the Assessing Officer on the basis of the assertions made by the assessee before him in the appellate proceedings and with reference to the material adduced by him, being the wealth-tax return for the assessment year 1990-91, and in relation to the construction of a new residential house, similarly named, on an adjacent piece of land. The same, to our mind, is misdirected, as the said material was not before the Assessing Officer at the time of original assessment, so that, irrespective of the validity of the assessee's claims, what is to be seen is whether he has made at the time of original assessment a full and proper disclosure of all material facts. In fact, the verification as directed, relates to pertinent facts only, and which only bears out to the absence of adequate material on record to support the assessee's claims. Further, the permission from the appropriate authority, for the sale of the capital asset(s) under reference, and which stands sought by the assessee himself, state of the same as an agricultural land, i.e., as described in the conveyance deed, which being a part of the original return ; it was held by him that there has been a full and true disclosure, with no new information or document coming to the notice of the Assessing Officer for initiation of reassessment proceedings. We find that to be a contradiction in terms, firstly, the assessee has not pleaded of the submission of the said permission at the time of the original assessment proceedings before the Assessing Officer. Secondly, even so, the same stating the subject-matter of the purported transfer to be an agricultural land, in agreement with the conveyance deed, the primary document transferring the title, while the assessee contends it to be only a

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residential house, an explanation for this contrary view is incumbent on the assessee, being a primary and material factual matter, i.e., if it were to be stated, as contended, that there is a full and true disclosure of all material facts, and which has it clearly failed to. This is more so considering that he has claimed deduction under sections which were only applicable for capital gains arising on a transfer of residential property. Thirdly, this becomes unarguably so as the *Explanation 1* to the proviso to section 147 clearly obliges the assessee to make an explicit/express disclosure, as against an implicit or a covert one.

As observed earlier, the return of income as furnished, and the claim(s) made as per it, is apparently inconsistent with the conveyance deed, which is the primary document in relation to the subject matter of transfer under reference, conveying the title to the capital asset as well as evidencing its character (and which in the facts of the case is based on its actual user), so that it cannot be said that there is a true and full disclosure of the material facts relevant for assessment by the assessee, and would, besides, warrant an explanation as referred to earlier (at para 5.2 above) and which the assessee pleads in the reassessment proceedings, placing reliance for the purpose on the decision in the case of *Hajee Mohamed Ibrahim* v. *GTO* (supra) and *CWT* v. *Smt. Azizunnisa Begum* (supra). In fact, the said decisions also ; the land, or a good part of it, being put to agricultural operations, prima facie support the Revenue's case, and not of the assessee. There is no expression of opinion in the original assessment order in the matter to hold it as a case of change of opinion.

5.7 In view of the foregoing, we are of the unequivocal view that there has not been a full and true disclosure of all material facts necessary for his assessment for the current assessment year by the assessee, so that the initiation of reassessment proceedings, the law in the matter being patently clear, by the issue of notice under section 148 of the Act, is not bad in law, as held by the first appellate authority.

5.8 The learned Commissioner of Income-tax (Appeals) has not decided the issue on merits as he had annulled the reassessment as made. Under the circumstances, having upheld the validity of the reassessment proceeding, the matter would necessarily have to go back to his file for adjudication on merits, which also stand agitated before him as per the grounds of appeal as enumerated at page 2 of his order. We decide accordingly."

4 Being dissatisfied with the order passed by the Appellate Tribunal, the assessee has come up with the present appeal.

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5 On April 29, 2009, this court admitted the appeal on the following two substantial questions of law :

> "(i) Whether on the facts and in the circumstances of the case, the Income-tax Appellate Tribunal was right in holding that the reopening of the assessment was rightly made ?
>
> (ii) Whether on the facts and in the circumstances of the case, the Income-tax Appellate Tribunal was right in holding that the assessee had not made full and true disclosure of all material facts necessary for his assessment ?"

6 Mr. Soparkar, the learned counsel appearing for the appellant, vehemently submitted that the Appellate Tribunal committed a serious error in passing the impugned order. He would submit that the Appellate Tribunal ought not to have disturbed the well-reasoned order passed by the Commissioner of Income-tax (Appeals). According to Mr. Soparkar, it cannot be said by any stretch of imagination that there was no full and true disclosure. According to Mr. Soparkar, there was no tangible material before the Assessing Officer for the purpose of reopening the assessment. The case is one of mere "change of opinion". In such circumstances referred to above, Mr. Soparkar prays that there being merit in his appeal, the same be allowed and the substantial questions of law as formulated by this court be answered in favour of the assessee and against the Revenue.

7 On the other hand, Ms. Mauna Bhatt, the learned standing counsel appearing for the Revenue, has vehemently opposed this appeal. Ms. Bhatt would submit that no error, not to speak of any error of law, could be said to have been committed by the Appellate Tribunal in passing the impugned order.

8 Ms. Bhatt would submit that the assessee could be said to have sold an agricultural land and not a residential house. The assessee is not entitled to claim deduction under sections 53(b) and 54(1)(i) of the Act. According to Ms. Bhatt, there was no full and true disclosure of the particulars and, therefore, the Assessing Officer was justified in reopening the assessment.

9 Having heard the learned counsel appearing for the parties and having gone through the materials on record, the only question that falls for our consideration is, whether the Appellate Tribunal committed any error in passing the impugned order.

10 We take notice of the fact that at many places in the deed of conveyance there is a reference of bungalow situated on the land bearing block No. 518. It is not in dispute that the assessee had filled in Form No. 37-I as provided in rule 48 of the Income-tax Rules. In the said form, there is a

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specific reference of a farmhouse along with water tank, servant quarter, etc. Form 37-I reads thus :

"Form No. 37-I

(*See rule 48L*)

Statement of transfer of immovable property to be furnished to the appropriate authority under section 269UC

I/We, ... intend to transfer the immovable property located at . . . . to . . . . The total apparent consideration for the transfer of the above property is . . . . The particulars of the agreement for transfer of the said property are furnished in the annexure to the statement.

Verification

In my/our opinion and to the best of my/our knowledge and information, the particulars furnished above and in the annexure hereto are true and correct.

Transferor(s)	Transferee(s)
1..	1.. . . . .
2..	2.. . . . .
3..	3.. . . . .

*Note : Any change in the address of the transferor(s) or the transferee(s) should be communicated in writing immediately to the appropriate authority to whom this statement of transfer has been furnished."

11 Section 53 of the Act reads thus :

"53. *Exemption of capital gains from a residential house.*—Notwithstanding anything contained in section 45, where in the case of an assessee being an individual or a Hindu undivided family, the capital gain arises from the transfer of long-term capital asset, being buildings or lands appurtenant thereto, and being a residential house, the income of which is chargeable under the head 'Income from house property', the capital gains arising from such transfer shall be dealt with in accordance with the following provisions of this section, that is to say,—

(a) in a case where the full value of the consideration received or accruing as a result of the transfer of such capital asset does not exceed two hundred thousand rupees the whole of the capital gain shall not be charged under section 45 ;

(b) in a case where the full value of such consideration exceeds two hundred thousand rupees, so much of the capital gain as bears to the whole of the capital gain the same proportion as the amount of

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two hundred thousand rupees bears to such consideration shall not be charged under section 45 :

Provided that nothing contained in this section shall apply to a case where the assessee owns on the date of such transfer any other residential house.

Explanation.—In this section and in sections 54, 54B, 54D, 54E, 54F and 54G, references to capital gain shall be construed as references to the amount of capital gain as computed under clause (a) of sub-section (1) of section 48."

12 Section 54(1)(i) of the Act reads thus :

"54. *Profit on sale of property used for residence*.—. . .

(i) if the amount of the capital gain is greater than the cost of the residential house so purchased or constructed (hereinafter in this section referred to as the new asset), the difference between the amount of the capital gain and the cost of the new asset shall be charged under section 45 as the income of the previous year ; and for the purpose of computing in respect of the new asset any capital gain arising from its transfer within a period of three years of its purchase or construction, as the case may be, the cost shall be nil ; or"

13 The principles of law governing reassessment may be summarised thus :

"(i) The court should be guided by the reasons recorded for the reassessment and not by the reasons or explanation given by the Assessing Officer at a later stage in respect of the notice of reassessment. To put it in other words, having regard to the entire scheme and the purpose of the Act, the validity of the assumption of jurisdiction under section 147 can be tested only by reference to the reasons recorded under section 148(2) of the Act and the Assessing Officer is not authorised to refer to any other reason even if it can be otherwise inferred or gathered from the records. The Assessing Officer is confined to the recorded reasons to support the assumption of jurisdiction. He cannot record only some of the reasons and keep the others up to his sleeves to be disclosed before the court if his action is ever challenged in a court of law.

(ii) At the time of the commencement of the reassessment proceedings, the Assessing Officer has to see whether there is prima facie material, on the basis of which, the Department would be justified in reopening the case. The sufficiency or correctness of the material is not a thing to be considered at that stage.

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(iii) The validity of the reopening of the assessment shall have to be determined with reference to the reasons recorded for reopening of the assessment.

(iv) The basic requirement of law for reopening of the assessment is application of mind by the Assessing Officer, to the materials produced prior to the reopening of the assessment, to conclude that he has reason to believe that income has escaped assessment. Unless that basic jurisdictional requirement is satisfied—a post-mortem exercise of analysing the materials produced subsequent to the reopening will not make an inherently defective reassessment order valid.

(v) The crucial link between the information made available to the Assessing Officer and the formation of the belief should be present. The reasons must be self evident, they must speak for themselves.

(vi) The tangible material which forms the basis for the belief that income has escaped assessment must be evident from a reading of the reasons. The entire material need not be set out. To put it in other words, something therein, which is critical to the formation of the belief must be referred to. Otherwise, the link would go missing.

(vii) The reopening of assessment under section 147 is a potent power and should not be lightly exercised. It certainly cannot be invoked casually or mechanically.

(viii) If the original assessment is processed under section 143(1) of the Act and not section 143(3) of the Act, the proviso to section 147 will not apply. In other words, although the reopening may be after the expiry of four years from the end of the relevant assessment year, yet it would not be necessary for the Assessing Officer to show that there was any failure to disclose fully or truly all the material facts necessary for the assessment.

(ix) In order to assume jurisdiction under section 147 where assessment has been made under sub-section (3) of section 143, two conditions are required to be satisfied :

(i) The Assessing Officer must have reason to believe that the income chargeable to tax has escaped assessment ;

(ii) Such escapement occurred by reason of failure on the part of the assessee either (a) to make a return of income under section 139 or in response to the notice issued under sub-section (1) of section 142 or section 148 or (b) to disclose fully and truly all the material facts necessary for his assessment for that purpose.

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(x) The Assessing Officer, being a quasi-judicial authority, is expected to arrive at a subjective satisfaction independently on an objective criteria.

(xi) While the report of the Investigation Wing might constitute the material, on the basis of which, the Assessing Officer forms the reasons to believe, the process of arriving at such satisfaction should not be a mere repetition of the report of the investigation. The reasons to believe must demonstrate some link between the tangible material and the formation of the belief or the reason to believe that the income has escaped assessment.

(xii) Merely because certain materials which is otherwise tangible and enables the Assessing Officer to form a belief that the income chargeable to tax has escaped assessment, formed part of the original assessment record, per se would not bar the Assessing Officer from reopening the assessment on the basis of such material. The expression 'tangible material' does not mean the material alien to the original record.

(xiii) The order, disposing of objections or any counter-affidavit filed during the writ proceedings before the court cannot be substituted for the 'reasons to believe'.

(xiv) The decision to reopen the assessment on the basis of the report of the Investigation Wing cannot always be condemned or dubbed as a fishing or roving inquiry. The expression 'reason to believe' appearing in section 147 suggests that if the Income-tax Officer acts as a reasonable and prudent man on the basis of the information secured by him that there is a case for reopening, then section 147 can well be pressed into service and the assessments be reopened. As a consequence of such reopening, certain other facts may come to light. There is no bar or any legal embargo under section 147 for the Assessing Officer to take into consideration such facts which come to light either by discovery or by a fuller probe into the matter and reassess the assessee in detail if circumstances require.

(xv) The test of jurisdiction under section 143 of the Act is not the ultimate result of the inquiry but the test is whether the Income-tax Officer entertained a 'bona fide' belief upon the definite information presented before him. Power under this section cannot be exercised on mere rumours or suspicions.

(xvi) The concept of 'change of opinion' has been treated as an inbuilt test to check abuse. If there is tangible material showing

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escapement of income, the same would be sufficient for reopening the assessment.

(xvii) It is not necessary that the Income-tax Officer should hold a quasi-judicial inquiry before acting under section 147. It is enough if he on the information received believes in good faith that the assessee's profits have escaped assessment or have been assessed at a low rate. However, nothing would preclude the Income-tax Officer from conducting any formal inquiry under section 133(6) of the Act before proceeding for reassessment under section 147 of the Act.

(xviii) The 'full and true' disclosure of the material facts would not include that material, which is to be used for testing the veracity of the particulars mentioned in the return. All such facts would be expected to be elicited by the Assessing Officer during the course of the assessment. The disclosure required only reference to those material facts, which if not disclosed, would not allow the Assessing Officer to make the necessary inquiries.

(xix) The word 'information' in section 147 means instruction or knowledge derived from the external source concerning the facts or particulars or as to the law relating to a matter bearing on the assessment. An information anonymous is information from unknown authorship but none the less in a given case, it may constitute information and not less an information though anonymous. This is now a recognized and accepted source for detection of large scale tax evasion. The non-disclosure of the source of the information, by itself, may not reduce the credibility of the information. There may be good and substantial reasons for such anonymous disclosure, but the real thing to be looked into is the nature of the information disclosed, whether it is a mere gossip, suspicion or rumour. If it is none of these, but a discovery of fresh facts or of new and important matters not present at the time of the assessment, which appears to be credible to an honest and rational mind leading to a scrutiny of facts indicating incorrect allowance of the expense, such disclosure would constitute information as contemplated in clause (b) of section 147.

(xx) The reasons recorded or the material available on record must have nexus to the subjective opinion formed by the Assessing Officer regarding the escapement of the income but then, while recording the reasons for the belief formed, the Assessing Officer is not required to finally ascertain the factum of escapement of the tax and it is sufficient that the Assessing Officer had cause or justification to know or suppose that the income had escaped assessment (vide *Rajesh Jhaveri*

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Stock Brokers (P.) Ltd. v. *Asst. CIT* [2006] 284 ITR 593 (Guj)). It is also well settled that the sufficiency and adequacy of the reasons which have led to the formation of a belief by the Assessing Officer that the income has escaped the assessment cannot be examined by the court."

14 Mr. Soparkar seeks to rely upon a decision of this court in the case of *Nilamben Sandipbhai Parikh* v. *Asst. CIT* [2019] 14 ITR-OL 587 (Guj) ; [2019] 109 taxmann.com 336 (Guj). We quote the relevant observations relied upon by Mr. Soparkar thus (page 591 of 14 ITR-OL) :

"Short question which arises for determination in this petition is, whether the concept of 'change of opinion' stands obliterated with effect from April 1, 1989, i.e., after substitution of section 147 of the Income-tax Act, 1961 by Direct Tax Laws (Amendment) Act, 1987 ?

To answer the above question, we need to note the changes undergone by section 147 of the Income-tax Act, 1961 (for short, 'the Act'). Prior to Direct Tax Laws (Amendment) Act, 1987, section 147 reads as under :

'147. *Income escaping assessment*.—If—

(a) the Income-tax Officer has reason to believe that, by reason of the omission or failure on the part of an assessee to make a return under section 139 for any assessment year to the Income-tax Officer or to disclose fully and truly all material facts necessary for his assessment for that year, income chargeable to tax has escaped assessment for that year, or

(b) notwithstanding that there has been no omission or failure as mentioned in clause (a) on the part of the assessee, the Income-tax Officer has in consequence of information in his possession reason to believe that income chargeable to tax has escaped assessment for any assessment year,

he may, subject to the provisions of sections 148 to 153, assess or reassess such income or recompute the loss or the depreciation allowance, as the case may be, for the assessment year concerned (hereafter in sections 148 to 153 referred to as the relevant assessment year).'

6.2.1 After enactment of Direct Tax Laws (Amendment) Act, 1987, i.e., prior to 1st April, 1989, section 147 of the Act, reads as under :

'147. *Income escaping assessment*.—If the Assessing Officer, for reasons to be recorded by him in writing, is of the opinion that any income chargeable to tax has escaped assessment for any assessment

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year, he may, subject to the provisions of sections 148 to 153, assess or reassess such income and also any other income chargeable to tax which has escaped assessment and which comes to his notice subsequently in the course of the proceedings under this section, or recompute the loss or the depreciation allowance or any other allowance, as the case may be, for the assessment year concerned (hereafter in this section and in sections 148 to 153 referred to as the relevant assessment year).'

6.2.3 After the Amending Act, 1989, section 147 reads as under :

'147. *Income escaping assessment*.—If the Assessing Officer has reason to believe that any income chargeable to tax has escaped assessment for any assessment year, he may, subject to the provisions of sections 148 to 153, assess or reassess such income and also any other income chargeable to tax which has escaped assessment and which comes to his notice subsequently in the course of the proceedings under this section, or recompute the loss or the depreciation allowance or any other allowance, as the case may be, for the assessment year concerned (hereafter in this section and in sections 148 to 153 referred to as the relevant assessment year).'

6.3 Considering the above, the apex court in the case of *CIT* v. *Kelvinator of India Ltd.* [2010] 320 ITR 561 (SC) observed and held in para 4 as under (page 564 of 320 ITR) :

'On going through the changes, quoted above, made to section 147 of the Act, we find that, prior to the Direct Tax Laws (Amendment) Act, 1987, reopening could be done under the above two conditions and fulfilment of the said conditions alone conferred jurisdiction on the Assessing Officer to make a back assessment, but in section 147 of the Act (with effect from April 1, 1989), they are given a go-by and only one condition has remained, viz., that where the Assessing Officer has reason to believe that income has escaped assessment, confers jurisdiction to reopen the assessment. Therefore, post-April 1, 1989, power to reopen is much wider. However, one needs to give a schematic interpretation to the words "reason to believe" failing which, we are afraid, section 147 would give arbitrary powers to the Assessing Officer to reopen assessments on the basis of "mere change of opinion", which cannot be per se reason to reopen. We must also keep in mind the conceptual difference between power to review and power to reassess. The Assessing Officer has no power to review ; he has the power to reassess. But reassessment has to be based on fulfilment of certain preconditions and if the concept of

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"change of opinion" is removed, as contended on behalf of the Department, then, in the garb of reopening the assessment, review would take place. One must treat the concept of "change of opinion" as an in-built test to check abuse of power by the Assessing Officer. Hence, after April 1, 1989, the Assessing Officer has power to reopen, provided there is "tangible material" to come to the conclusion that there is escapement of income from assessment. Reasons must have a live link with the formation of the belief. Our view gets support from the changes made to section 147 of the Act, as quoted hereinabove. Under the Direct Tax Laws (Amendment) Act, 1987, Parliament not only deleted the words "reason to believe" but also inserted the word "opinion" in section 147 of the Act. However, on receipt of representations from the companies against omission of the words "reason to believe", Parliament reintroduced the said expression and deleted the word "opinion" on the ground that it would vest arbitrary powers in the Assessing Officer. We quote hereinbelow the relevant portion of Circular No. 549 dated October 31, 1989 ([1990] 182 ITR (St.) 1, 29), which reads as follows :

"7.2 *Amendment made by the Amending Act, 1989, to reintroduce the expression 'reason to believe' in section 147.*—A number of representations were received against the omission of the words 'reason to believe' from section 147 and their substitution by the 'opinion' of the Assessing Officer. It was pointed out that the meaning of the expression, 'reason to believe' had been explained in a number of court rulings in the past and was well settled and its omission from section 147 would give arbitrary powers to the Assessing Officer to reopen past assessments on mere change of opinion. To allay these fears, the Amending Act, 1989, has again amended section 147 to reintroduce the expression 'has reason to believe' in place of the words 'for reasons to be recorded by him in writing, is of the opinion'. Other provisions of the new section 147, however, remain the same."

For the aforestated reasons, we see no merit in these civil appeals filed by the Department ; hence, dismissed with no order as to costs.'

6.4 Even this court in the case of *Giriraj Steel* (supra) has held that reopening of assessment being based on a mere change of opinion, the assumption of jurisdiction on the part of the Assessing Officer lacks validity and the notice under section 148 of the Act cannot be sustained.

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6.5 The Assessing Officer has power to reopen the assessment, provided there is 'tangible material' to come to the conclusion that there is escapement of income from assessment and the reasons must have a live link with the formation of belief. In the present case, there is no tangible material. The issuance of the impugned notice under section 148 is nothing but mere change of opinion. In the absence of any new tangible material available with the Assessing Officer, it is not open to the Assessing Officer to change his opinion by issuing the notice of reassessment.

6.6 From the reasons recorded it can be said that the original assessment is sought to be reopened in exercise of powers under section 147/148 of the Act on change of opinion by the Assessing Officer, which is not permissible more particularly when the original assessment is sought to be reopened after a period of four years from the end of the assessment year. Under the circumstances, the conditions stipulated under first proviso to section 147 are not satisfied and therefore, on the aforesaid ground alone, the impugned notice deserves to be quashed and set aside."

15 Thus, having regard to the position of law and the materials emerging from the record of the case, it cannot be said that there was no full and true disclosure at the end of the assessee of the material facts. In such circumstances, it could be said that there was no tangible material with the Assessing Officer for the purpose of reopening the assessment except the change of opinion that the deductions could not have been claimed and allowed under sections 53(b) and 54(1)(i) of the Act. The conveyance deed, permission of the appropriate authority to sell the property and other documents were filed by the appellant at the time of original assessment proceedings. Nothing was suppressed. Form 37-I as referred to above speaks for itself. It is not in dispute that the notice under section 148 of the Act came to be issued beyond the period of four years. The Commissioner of Income-tax (Appeals) recorded a finding of fact that there was no failure on the part of the assessee to disclose fully and truly all the material facts necessary for the assessment. Such finding of fact could not have been disturbed by the Appellate Tribunal without any basis for the same.

16 The Supreme Court in the case of *Omar Salay Mohamed Sait* v. *CIT* [1959] 37 ITR 151 (SC), succinctly expressed the expectation from a Tribunal while deciding the appeals. The following observations are important :

"We are aware that the Income-tax Appellate Tribunal is a fact finding Tribunal and if it arrives at its own conclusions of fact after

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due consideration of the evidence before it this court will not interfere. It is necessary, however, that every fact for and against the assessee must have been considered with due care and the Tribunal must have given its finding in a manner which would clearly indicate what were the questions which arose for determination, what was the evidence pro and contra in regard to each one of them and what were the findings reached on the evidence on record before it. The conclusions reached by the Tribunal should not be coloured by any irrelevant considerations or matters of prejudice and if there are any circumstances which required to be explained by the assessee, the assessee should be given an opportunity of doing so. On no account whatever should the Tribunal base its findings on suspicions, conjectures or surmises nor should it act on no evidence at all or on improper rejection of material and relevant evidence or partly on evidence and partly on suspicions, conjectures or surmises and if it does anything of the sort, its findings, even though on questions of fact, will be liable to be set aside by the court."

17 In view of the aforesaid, we hold that the impugned order passed by the Appellate Tribunal is not sustainable in law.

18 In the result, this appeal succeeds and is hereby allowed. The impugned order passed by the Income-tax Appellate Tribunal, Ahmedabad Bench "D" dated March 9, 2007 in I. T. A. No. 1113/Ahd/2001 for the assessment year 1991-92 is hereby quashed and set aside. The two substantial questions of law as formulated by this court are answered in favour of the appellant-assessee and against the Revenue.

[2020] 425 ITR 99 (Ker)

[IN THE KERALA HIGH COURT]

BEAVER ESTATES PVT. LTD. AND ANOTHER

v.

ASSISTANT COMMISSIONER OF INCOME-TAX AND OTHERS

R. NARAYANA PISHARADI J.

October 23, 2019.

SS ▸ ITA 1961, s 276C(1) ; Constn of India, art 227
HF ▸ Assessee

OFFENCES AND PROSECUTION—EVASION OF TAX—ASSESSEE'S APPEAL AGAINST ASSESSMENT PENDING BEFORE STATUTORY AUTHORITY—WRIT

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PETITION—CRIMINAL PROCEEDINGS TO BE KEPT IN ABEYANCE TILL DECISION IN STATUTORY APPEAL—INCOME-TAX ACT, 1961, S. 276C(1)—CONSTITUTION OF INDIA, art. 227.

A complaint was filed against the assessee-company and its managing director by the Assistant Commissioner alleging wilful attempt to evade tax punishable under section 276C(1) of the Income-tax Act, 1961. On a writ petition, by the assessees contending that they had filed an appeal before the statutory authority challenging the assessment and that the criminal proceedings pending against them might be kept in abeyance till disposal of the statutory appeal :

Held, *allowing the petition, that there was force in the contention of the assessees that the appeal before the statutory appellate authority regarding the assessment and the computation of the tax would have a bearing on the prosecution against the assessees for wilful attempt to evade tax. The Additional Chief Judicial Magistrate (Economic Offences) was directed to keep in abeyance all further proceedings against the assessees.*

K. C. BUILDERS *v.* ASST. CIT [2004] 265 ITR 562 (SC) *and* CIT *v.* BHUPEN CHAMPAK LAL DALAL [2001] 248 ITR 830 (SC) *applied.*

SASI ENTERPRISES *v.* ASST. CIT [2014] 361 ITR 163 (SC) *distinguished.*

Cases referred to :

CIT *v.* Bhupen Champak Lal Dalal [2001] 248 ITR 830 (SC) (para 7)
K. C. Builders *v.* Asst. CIT [2004] 265 ITR 562 (SC) (para 5)
Sasi Enterprises *v.* Asst. CIT [2014] 361 ITR 163 (SC) (para 9)

O. P. (Crl.) No. 400 of 2019.

Dale P. Kurien for the petitioners.

Jose Joseph, Standing Counsel for the Income-tax Department, for respondent No. 1 and Public Prosecutor for respondent No. 3.

JUDGMENT

1 R. NARAYANA PISHARADI J.—This original petition is filed under article 227 of the Constitution of India. The prayer in this petition is to issue a direction to the Additional Chief Judicial Magistrate's Court (Economic Offences), Ernakulam to keep in abeyance all further proceedings in the case C. C. No. 65 of 2015 of that court till the disposal of the appeal filed by the petitioners in the matter before the Commissioner of Income-tax (Appeals).

2 The petitioners are the accused in the aforesaid case. The first petitioner is a company. The second petitioner is the managing director of the first petitioner-company. The case C. C. No. 65 of 2015 is based on the com-

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plaint filed against them by the Assistant Commissioner of Income-tax alleging that they had made wilful attempt to evade tax and that they have committed the offence punishable under section 276C(1) of the Income-tax Act, 1961 (hereinafter referred to as "the Act").

3 The plea of the petitioners is that they have filed appeal before the statutory authority challenging the assessment of tax and that the decision in the appeal has got a bearing on the prosecution against them and therefore, the criminal proceedings pending against them may be kept in abeyance till the disposal of the aforesaid appeal.

4 Heard learned counsel for the petitioners and the learned standing counsel for the Government of India (Taxes) and the learned Public Prosecutor.

5 Learned counsel for the petitioners contended that, if the statutory appeal filed by the petitioners under the Act is allowed, it would knock down the very basis of the prosecution against them and therefore, the criminal proceedings may be ordered to be kept in abeyance. Learned counsel for the petitioners has relied upon the decision of the apex court in *K. C. Builders* v. *Asst. CIT* [2004] 265 ITR 562 (SC) ; [2004] 2 SCC 731 in support of his contention.

6 There is force in the aforesaid contention. *K. C. Builders* (supra) was a case of concealment of income where penalty was imposed on the assessee by the assessing authority. The prosecution against the assessee was under sections 276C(2) and 278B of the Act and sections 193, 196 and 420 and 120B of the Indian Penal Code. Section 276C of the Act provides the punishment for wilful attempt to evade tax, penalty or interest. Section 278B of the Act provides for offences by companies. In *K. C. Builders* (supra), the apex court has held that the levy of penalties and the prosecution under section 276C of the Act are simultaneous and hence, once the penalties are cancelled on the ground that there is no concealment, the quashing of prosecution under section 276C of the Act is automatic. In the instant case, the prosecution is under section 276C(1) of the Act for wilful attempt to evade tax. The decision of the statutory appellate authority regarding the assessment and computation of tax would have a bearing on the prosecution against the petitioners.

7 Learned counsel for the petitioners has also relied upon the decision of the Supreme Court in *CIT* v. *Bhupen Champak Lal Dalal* [2001] 248 ITR 830 (SC) ; AIR 2001 SC 1096, wherein it has been held as follows (page 832 of 248 ITR) :

> "The prosecution in criminal law and proceedings arising under the Act are undoubtedly independent proceedings and, therefore,

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there is no impediment in law for the criminal proceedings to proceed even during the pendency of the proceedings under the Act. However, a wholesome rule will have to be adopted in matters of this nature where courts have taken the view that when the conclusions arrived at by the appellate authorities have a relevance and bearing upon the conclusions to be reached in the case necessarily one authority will have to await the outcome of the other authority."

8 The decision in *Bhupen Champak Lal Dalal* (supra) has also got application in the instant case because the decision of the statutory appellate authority regarding the assessment and computation of tax would have a bearing on the prosecution against the petitioners for wilful attempt to evade tax.

9 Learned standing counsel for the first and the second respondents has invited the attention of this court to the decision of the apex court in *Sasi Enterprises* v. *Asst. CIT* [2014] 361 ITR 163 (SC) ; [2014] 5 SCC 139, wherein it has been held as follows (page 179 of 361 ITR) :

"We also find no basis in the contention of the learned senior counsel for the appellant that pendency of the appellate proceedings is a relevant factor for not initiating prosecution proceedings under section 276CC of the Act. Section 276CC contemplates that an offence is committed on the non-filing of the return and it is totally unrelated to the pendency of assessment proceedings except for second part of the offence for determination of the sentence of the offence, the Department may resort to best judgment assessment or otherwise to past years to determine the extent of the breach . . . If it was the intention of the Legislature to hold up the prosecution proceedings till the assessment proceedings are completed by way of appeal or otherwise the same would have been provided in section 276CC itself. Therefore, the contention of the learned senior counsel for the appellant that no prosecution could be initiated till the culmination of the assessment proceedings, especially in a case where the appellant had not filed the return as per section 139(1) of the Act or following the notices issued under section 142 or section 148 does not arise."

10 The decision in *Sasi Enterprises* (supra) has got no application to the present case because the prosecution against the petitioners is for committing the offence under section 276C of the Act and not for the offence under section 276CC of the Act.

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True, today itself, I have dismissed two other petitions filed for identical relief. But, in those petitions, the prosecution against the petitioners is under section 276CC of the Act and not under section 276C of the Act. **11**

In the aforesaid circumstances, in the light of the decision of the apex court in *Bhupen Champak Lal Dalal* (supra), I find that this is a fit case where the supervisory jurisdiction of this court under article 227 of the Constitution should be invoked to issue appropriate direction to the lower court. **12**

In the result, the petition is allowed. The Additional Chief Judicial Magistrate (Economic Offences), Ernakulam is directed to keep in abeyance all further proceedings against the petitioners in the case C. C. No. 65 of 2015 of that court till the disposal of I. T. A. No. 28/R-1/CIT(A)-II/15-16 filed by them before the Commissioner of Income-tax (Appeals), Kochi. **13**

[2020] 425 ITR 103 (Guj)

[IN THE GUJARAT HIGH COURT]

KAKARIA HOUSING AND INFRASTRUCTURE LTD.

v.

DEPUTY COMMISSIONER OF INCOME-TAX

MS. HARSHA DEVANI and MS. SANGEETA K. VISHEN JJ.

October 7, 2019.

SS ▸ ITA 1961, ss 147, 148
AY ▸ 2012-13
HF ▸ Assessee

REASSESSMENT—NOTICE AFTER FOUR YEARS—VALIDITY—FAILURE TO DISCLOSE MATERIAL FACTS NECESSARY FOR ASSESSMENT—SCRUTINY ASSESSMENT—NO NEW MATERIAL—AUDIT OBJECTIONS NOT ACCEPTED BY ASSESSING OFFICER—BELIEF BY ASSESSING OFFICER THAT INCOME CHARGEABLE TO TAX HAS ESCAPED ASSESSMENT NOT HIS OWN—NOTICE NOT VALID—INCOME-TAX ACT, 1961, SS. 147, 148.

When during the original assessment a claim has been processed at length and after calling for detailed explanation it has been accepted, merely because a certain element or angle was not in the mind of the Assessing Officer while accepting such a claim, it cannot be a ground for issuing notice under section 148 of the Income-tax Act, 1961.

Though an audit objection may serve as information on the basis of which the Income-tax Officer can act to reopen an assessment, the ultimate action

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must depend directly and solely on the formation of belief by the Income-tax Officer on his own where such information is passed on to him by the audit that income has escaped assessment.

Held, *that the assessee was engaged in the business of real estate development. In respect of the provision for future development expenses made by the assessee, the Assessing Officer had called for an explanation and after considering it, had accepted it. As regards the other issue, namely the provision for future development expenses, the assessment was sought to be reopened merely for examining the same issue from a different angle. Therefore, on both counts the reassessment would amount to mere change of opinion on the part of the Assessing Officer and hence, the assumption of jurisdiction on the part of the Assessing Officer under section 147 of the Act lacked validity. Moreover, the assessment of the assessee was sought to be reopened after a period of more than four years from the end of the relevant assessment year. On a plain reading of the reasons recorded, it was evident that all the facts were already before the Assessing Officer at the time of scrutiny assessment and no fresh material had been relied upon by him for the purpose of reopening the assessment. The reasons for the notice of reassessment revealed that the Audit Department had raised objections in respect of both the issues on which the assessment was sought to be reopened. On both the counts, the Assessing Officer did not accept the objections and gave his explanation for not accepting them. However, the audit department found the reply of the Assessing Officer not tenable. Evidently, therefore, the formation of belief that income chargeable to tax had escaped assessment was not that of the Assessing Officer, but was based upon the borrowed satisfaction of the audit department. The notice of reassessment was not valid.*

Cases referred to :

Adani Exports *v.* Deputy CIT (Assessments) [1999] 240 ITR 224 (Guj) (para 6)

Adani Infrastructure and Developers (P.) Ltd. *v.* Asst. CIT [2019] 101 taxmann.com 256 (Guj) (para 6)

Cliantha Research Ltd. *v.* Deputy CIT [2013] 35 taxmann.com 61 (Guj) (para 6)

ITO *v.* Techspan India Private Ltd. [2018] 404 ITR 10 (SC) (para 6)

Indian and Eastern Newspaper Society *v.* CIT [1979] 119 ITR 996 (SC) (para 19)

R/Special Civil Application No. 16767 of 2018.

Hardik V. Vora for the petitioner.

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Nikunt Raval, Advocate, for *Mrs. Kalpana K. Raval*, Senior Standing Counsel, for the respondent.

JUDGMENT[1]

The judgment of the court was delivered by

Ms. Harsha Devani J.—Rule. Mrs. Kalpana Raval, learned senior standing counsel, waives service of notice of rule on behalf of the respondent. **1**

Having regard to the controversy involved in the present case, which lies in a very narrow compass, the matter was taken up for final hearing today. **2**

By this petition under article 226 of the Constitution of India, the petitioner has challenged the notice dated March 23, 2018 issued by the respondent under section 148 of the Income-tax Act, 1961 (hereinafter referred to as "the Act") seeking to reopen the assessment of the petitioner for the assessment year 2012-13. **3**

The petitioner is engaged in the business of real estate development and is also a partner in M/s. Sai Royal Properties, which is engaged in the same business. The petitioner filed its return of income for the assessment year 2012-13 declaring total income at Rs. 3,17,74,860 on September 27, 2012. The case was selected for scrutiny, whereafter, by an order dated January 19, 2015, assessment came to be framed under section 143(3) of the Act assessing the income of the petitioner at Rs. 3,19,11,584 after making an addition of Rs. 1,36,725 under section 14A of the Act. **4**

Thereafter, by the impugned notice dated March 23, 2018, the respondent seeks to reopen the assessment of the petitioner for the assessment year 2012-13. By a letter dated April 12, 2018, the petitioner requested the respondent to accept the original return of income filed on September 27, 2012, as the return filed in response to the notice under section 148 of the Act. The petitioner electronically filed its return of income on April 20, 2018. The petitioner also requested the respondent to furnish the reasons recorded for reopening the assessment. It appears that in the meanwhile the petitioner had also made an application under the Right to Information Act, pursuant to which the Office of the Principal Director of Audit had given a detailed reply. A copy of the reasons recorded were furnished to the petitioner along with a letter dated July 23, 2018. The petitioner raised objections to the reopening of assessment with detailed submissions, which came to be rejected by an order dated October 16, 2018. **5**

Mr. Hardik Vora, learned advocate for the petitioner, submitted that in this case, the impugned notice dated March 23, 2018 has been issued in **6**

1. Oral judgment.

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relation to the assessment year 2012-13, which is clearly beyond a period of four years from the end of the relevant assessment year. Therefore, for the purpose of assuming jurisdiction under section 147 of the Act, there has to be failure on the part of the petitioner to disclose fully and truly all material facts necessary for its assessment for the assessment year under consideration. It was submitted that in the present case, all the facts relevant for assessment were duly placed before the Assessing Officer at the time of scrutiny assessment and hence, in the absence of any failure on the part of the petitioner to disclose fully and truly all material facts necessary for its assessment for the year under consideration, the assumption of jurisdiction on the part of the Assessing Officer is without authority of law.

6.1 The attention of the court was invited to the reasons recorded for reopening the assessment, to submit that the Assessing Officer seeks to reopen the assessment on two grounds, firstly, in relation to an amount of Rs. 2,47,62,500 shown by the petitioner in its return of income as capital gains on the ground that the same should have been assessed as income of the petitioner under section 28(iv) of the Act ; and secondly, that the petitioner had created a provision for future development expense of Rs. 3,59,48,400 and had debited the same under the head "Cost of materials", which was created on estimation basis and hence, this was a provision which was required to be added to the net profit for computing book profit as per the provisions of section 115JB of the Act.

6.2 Reference was made to the notice dated November 19, 2014 issued by the Assessing Officer under section 142(1) of the Act during the course of scrutiny assessment, to point out that he had specifically called upon the petitioner to state as to why the provision for future development expenses of Rs. 2,51,86,534 have been debited to the profit and loss account, but have not been added back in the computation of income and that the provision is not an expense incurred for the purpose of business and is unascertainable in nature. The petitioner was, accordingly, called upon to explain as to why such amount should not be added back to the return of income. It was pointed out that the petitioner was also called upon to explain as to why the gain on retirement from M/s. Sai Royal Properties should not be treated as business income given the fact that M/s. Sai Royal Properties was also engaged in the business as that of the petitioner and was essentially, an extension of the petitioner.

6.3 It was pointed out that in response to the notice under section 142(1) of the Act, the petitioner had given a detailed reply explaining the two issues raised by the Assessing Officer. It was submitted that the Assessing Officer, after being convinced with the explanation given by the

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petitioner, framed assessment under section 143(3) of the Act, without making any addition in respect of these two issues. It was submitted that therefore, during the course of scrutiny assessment, the Assessing Officer had duly applied his mind to both the issues on which the assessment is sought to be reopened and hence, the reopening is based on a mere change of opinion and therefore also, the assumption of jurisdiction on the part of the Assessing Officer lacks validity.

6.4 In support of his submissions, the learned advocate placed reliance upon the decision of the Supreme Court in the case of *ITO* v. *Techspan India Private Ltd.* [2018] 404 ITR 10 (SC) ; [2018] 92 taxmann.com 361 (SC), wherein the court held thus (page 18 of 404 ITR) :

> "The fact in controversy in this case is with regard to the deduction under section 10A of the Income-tax Act which was allegedly allowed in excess. The show-cause notice dated February 10, 2005 reflects the ground for reassessment in the present case, that is, the deduction allowed in excess under section 10A and, therefore, the income has escaped assessment to the tune of Rs. 57,36,811. In the order in question dated August 17, 2005, the reason purportedly given for rejecting the objections was that the assessee was not maintaining any separate books of account for the two categories, i.e., software development and human resource development, on which it has declared income separately. However, a bare perusal of notice dated March 9, 2004 which was issued in the original assessment proceedings under section 143 makes it clear that the point on which the reassessment proceedings were initiated, was well considered in the original proceedings. In fact, the very basis of issuing the show-cause notice dated March 9, 2004 was that the assessee was not maintaining any separate books of account for the said two categories and the details filed do not reveal proportional allocation of common expenses be made to these categories. Even the said show-cause notice suggested how proportional allocation should be done. All these things lead to an unavoidable conclusion that the question as to how and to what extent deduction should be allowed under section 10A of the Income-tax Act was well considered in the original assessment proceedings itself. Hence, initiation of the reassessment proceedings under section 147 by issuing a notice under section 148 merely because of the fact that now the Assessing Officer is of the view that the deduction under section 10A was allowed in excess, was based on nothing but a change of opinion on the same facts and circumstances which were

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already in his knowledge even during the original assessment proceedings."

6.5 Lastly, it was pointed out that pursuant to the application made by the petitioner under the Right to Information Act, 2005 the audit paras have been furnished to the petitioner. The attention of the court was invited to the audit paras to point out that both the issues, on which the Assessing Officer seeks to reopen the assessment, are based upon the objections raised by the audit department. Referring to the audit paras, it was pointed out that in response to both the issues, the Assessing Officer did not accept the objections and gave his reply thereto. However, the audit department did not accept the reply of the Assessing Officer. It was submitted that therefore, the formation of belief that income chargeable to tax has escaped assessment is not that of the Assessing Officer, but of the audit department and hence also, the reopening of assessment is bad.

6.6 To bolster his submission, learned advocate placed reliance upon the decision of this court in the case of *Adani Exports* v. *Deputy CIT (Assessments)* [1999] 240 ITR 224 (Guj), wherein it has been held thus (page 230 of 240 ITR) :

> "It is true that satisfaction of the Assessing Officer for the purpose of reopening is subjective in character and the scope of judicial review is limited. When the reasons recorded show a nexus between the formation of belief and the escapement of income, a further enquiry about the adequacy or sufficiency of the material to reach such belief is not open to be scrutinised. However, it is always open to question the existence of such belief on the ground that what has been stated is not the correct state of affairs existing on record. Undoubtedly, in the face of the record, the burden lies, and heavily lies, on the petitioner who challenges it. If the petitioner is able to demonstrate that in fact the Assessing Officer did not have any reason to believe or did not hold such belief in good faith or the belief which is projected in papers is not belief held by him in fact, the exercise of authority conferred on such person would be ultra vires the provisions of law and would be an abuse of such authority. As the aforesaid decision of the Supreme Court indicates though audit objection may serve as information on the basis of which the Income-tax Officer can act, ultimate action must depend directly and solely on the formation of belief by the Income-tax Officer on his own where such information is passed on to him by the audit that income has escaped assessment. In the present case, by scrupulously analysing the audit objection in great detail, the Assessing Officer has demonstrably shown to have held

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the belief prior to the issuance of notice as well as after the issuance of notice that the original assessment was not erroneous and so far as he was concerned, he did not believe at any time that income has escaped assessment on account of erroneous computation of benefit under section 80HHC. He has been consistent in his submission of his report to the superior officers. The mere fact that as a subordinate officer he added the suggestion that if his view is not accepted, remedial actions may be taken cannot be said to be belief held by him. He has no authority to surrender or abdicate his function to his superiors, nor the superiors can arrogate to themselves such authority. It needs hardly to be stated that in such circumstances the conclusion is irresistible that the belief that income has escaped assessment was not held at all by the officer having jurisdiction to issue notice and recording under the office note on February 8, 1997, that he has reason to believe is a mere pretence to give validity to the exercise of power. In other words, it was a colourable exercise of jurisdiction by the Assessing Officer by recording reasons for holding a belief which in fact demonstrably he did not hold that income of the assessee has escaped assessment due to erroneous computation of deduction under section 80HHC, for the reasons stated by the audit. The reason is not far to seek."

6.7 Reliance was also placed upon the decision of this court in the case of *Adani Infrastructure and Developers (P.) Ltd.* v. *Asst. CIT* [2019] 101 taxmann.com 256 (Guj), wherein the court has recorded that in the facts of the said case, the record clearly revealed that the Assessing Officer had not accepted the objections raised by the audit party and on the contrary, had objected to such objections by communicating internally. Evidently, therefore, the Assessing Officer had not formed any independent belief that income chargeable to tax had escaped assessment.

6.8 Reliance was also placed upon the decision of this court in the case of *Cliantha Research Ltd.* v. *Deputy CIT* [2013] 35 taxmann.com 61 (Guj), wherein it has been held that when during the original assessment the assessee's claim was processed at length and after calling for detailed explanation the same was accepted, merely because a certain element or angle was not in the mind of the Assessing Officer while accepting such a claim, it cannot be a ground for issuing notice under section 148 for reassessment.

6.9 It was, accordingly, urged that the petition deserves to be allowed by setting aside the impugned notice issued under section 148 of the Act as well as all proceedings taken pursuant thereto.

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7 Opposing the petition, Mr. Nikunt Raval learned advocate for Mrs. Kalpana Raval, learned senior standing counsel for the respondent, submitted that in so far as the addition of the provision for future development expenses to the net profit for computing book profit under section 115JB of the Act is concerned, the said amount was created on estimation basis, which was never disclosed at the time of the scrutiny assessment proceedings. The then Assessing Officer had discussed about the allowability of such claim as business expense, as the provision was not an expense for the purpose of business. It was submitted that the issue of allowability of such unascertainable expense while calculating book profit under section 115JB of the Act was never discussed during the original assessment proceedings and therefore, it cannot be said that the Assessing Officer had formed an opinion on this issue. Under the circumstances, it cannot be said that the reopening is based upon a mere change of opinion.

7.1 As regards the contention raised by the learned advocate for the petitioner that the reopening of assessment is based upon an audit objection, it was submitted that there is no mention of any audit objection in the reasons recorded for reopening the assessment. Therefore, the question of borrowed satisfaction on the part of the Assessing Officer while reopening the assessment would not arise. It was submitted that the Assessing Officer, after duly applying his mind to the facts of the case and forming the requisite belief that income chargeable to tax has escaped assessment, has assumed jurisdiction under section 147 of the Act and that there being no infirmity in the action of the respondent, there is no warrant for interference by this court.

8 This court has considered the submissions advanced by the learned advocates for the respective parties. As can be seen from the reasons recorded, the Assessing Officer seeks to reopen the assessment on the following two grounds, which are extracted for ready reference :

> "(i) The assessee-company was a partner in M/s. Sai Royal Properties having 50 per cent. share as partner. This share of capital was accounted by the assessee-company under the head 'Investments'. On retirement from the partnership firm, M/s. Sai Royal Properties, the assessee had received Rs. 2,47,62,500 from M/s. Sai Royal Properties in addition to its capital balance of Rs. 3,98,65,000. It had shown the amount of Rs. 2,47,62,500 in its return of income as capital gain, as the character of the investment is 'capital' in nature. However, on perusal of para 21 regarding 'settlement of account and goodwill', of the partnership deed of M/s. Sai Royal Properties, dated July 2, 2007, it is noticed that there it was specifically mentioned that

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the retiring partner would not be entitled to receive any amount as goodwill or otherwise beyond the balance standing to the credit of such party's capital account in the books of the firm after adjusting the share of profit and loss up to the date of retirement. Hence, the amount of Rs. 2,47,62,500 received by the assessee should have been treated as income of the assessee under section 28(iv) of the Income-tax Act.

(ii) The assessee-company was engaged in the business of real estate deve1opment, i.e., developing the property into sub-plots. For arriving at correct profit, every year the assessee estimated the cost required to be incurred to meet the promises made to the buyers of the plots and if required revised the estimates made earlier. For this, the assessee had created a provision for future development expense of Rs. 3,59,48,400 and debited the same under the head cost of materials. However, the same was created on an estimation basis, the liability for which was not ascertained during the year. As this was a provision, it was required to be added to the net profit for computing book profit as per the provisions of section 115JB. As per the provision of section 115JB of the Income-tax Act, profit as per profit and loss is to be increased by the amount set aside to provide for meeting liabilities, other than ascertained liabilities. Hence, Rs. 3,59,48,400 was required to be added to the net profit for computing book profit under section 115JB."

9 Thus, it is on the above referred two grounds that the Assessing Officer seeks to reopen the assessment of the petitioner for the assessment year under consideration. Since it has been contended on behalf of the petitioner that the reopening is based upon a mere change of opinion, it would be necessary to examine as to whether the Assessing Officer, at the time of scrutiny assessment, has applied his mind to the said issues. In this regard, a perusal of the notice dated November 19, 2014 issued under section 142(1) of the Act reveals that the Assessing Officer had specifically stated that the provision for future development expenses of Rs. 2,51,86,534 have been debited to the profit and loss account, but have not been added back to the computation of income ; and that the provision is not an expense incurred for the purpose of business and is unascertainable in nature. He had, accordingly, called upon the petitioner to explain as to why the said amount should not be added back to the returned income. The Assessing Officer had further called upon the petitioner to explain as to why the gain on retirement from firm, M/s. Sai Royal Properties should not be treated as

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business income, given the fact that M/s. Sai Royal Properties is engaged in the same business and is essentially an extension of the petitioner.

10 Thus, though not stated in exactly the same terms, the Assessing Officer did call for an explanation from the petitioner in respect of both the items on which the respondent seeks to reopen the assessment. Furthermore, in response to the notice issued by the Assessing Officer under section 142(1) of the Act, the petitioner had given its explanation by a communication which was received by the Assessing Officer on December 4, 2014, wherein both the issues have been explained at length. The Assessing Officer, after considering the explanation tendered by the petitioner, has not made any addition in respect of these two issues in the assessment framed under section 143(3) of the Act.

11 On behalf of the respondent, it has been contended that the issue of allowability of unascertainable expenses while calculating book profit under section 115JB of the Act was never discussed during the original proceedings and therefore, it cannot be said that the Assessing Officer has formed an opinion on this issue.

12 In this regard, it may be germane to refer to the decision of this court in the case of *Cliantha Research Ltd.* v. *Deputy CIT* (supra), wherein it has been held that when during original assessment the claim has been processed at length and after calling for detailed explanation the same was accepted, merely because a certain element or angle was not in the mind of the Assessing Officer while accepting such a claim, it cannot be a ground for issuing notice under section 148 of the Act.

13 In the facts of the present case, in respect of the provision for future development expenses made by the petitioner, the Assessing Officer had called for an explanation and after considering the same, had accepted it. Now, the respondent-Assessing Officer seeks to reopen the assessment for the purpose of examining it from another angle, namely the issue of allowability of such unascertainable expense while calculating book profit under section 115JB of the Act.

14 At this juncture, it may also be apposite to refer to the decision of the Supreme Court in the case of *ITO* v. *Techspan India Private Ltd.* (supra), wherein it has been held that initiation of reassessment proceedings under section 147 by issuing notice under section 148 merely because of the fact that now the Assessing Officer is of the view that deduction under section 10A was allowed in excess, was based on nothing but a change of opinion on the same facts and circumstances which were already in his knowledge even during the original assessment proceedings.

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15 In the opinion of this court, the above decisions would be squarely applicable to the facts of the present case inasmuch as in so far as the first issue is concerned, the Assessing Officer had called for details and after considering the explanation given by the assessee, had accepted the same. As regards the other issue, namely the provision for future development expenses, the assessment is sought to be reopened merely for examining the same issue from a different angle. Therefore, on both the counts on which the assessment is sought to be reopened, it would amount to mere change of opinion on the part of the Assessing Officer and hence, the assumption of jurisdiction on the part of the Assessing Officer under section 147 of the Act, lacks validity.

16 Another aspect of the matter is that the assessment of the petitioner is sought to be reopened after a period of more than four years from the end of the relevant assessment year. On a plain reading of the reasons recorded, it is evident that all facts were already before the Assessing Officer at the time of scrutiny assessment and no fresh material has been relied upon by the respondent for the purpose of reopening the assessment. Under the circumstances, it cannot be said that there is any failure on the part of the petitioner to disclose fully and truly all material facts necessary for its assessment. Under the circumstances, in the light of the first proviso to section 147 of the Act, the assumption of jurisdiction on the part of the respondent-Assessing Officer beyond a period of four years from the end of the relevant assessment year without there being any failure on the part of the petitioner to disclose fully and truly all material facts necessary for its assessment, is without authority of law.

17 Last but not the least, as pointed out by the learned advocate for the petitioner, the petitioner had obtained a copy of the audit para under the Right to Information Act, 2005. A perusal thereof reveals that the audit department had raised objections in respect of both the issues on which the assessment is sought to be reopened. On both the counts, the Assessing Officer did not accept the objections and gave his explanation for not accepting the same. However, the audit department found the reply of the Assessing Officer was not tenable. Evidently, therefore, the formation of belief that income chargeable to tax has escaped assessment is not that of the Assessing Officer, but is based upon the borrowed satisfaction of the audit department.

18 As held by this court in the case of *Adani Exports* v. *Deputy CIT (Assessments)* (supra), if the petitioner is able to demonstrate that in fact the Assessing Officer did not have any reason to believe or did not hold such belief in good faith or the belief which is projected in papers is not

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belief held by him in fact, the exercise of authority conferred on such person would be ultra vires the provisions of law and would be an abuse of such authority.

19 The Supreme Court, in the case of *Indian and Eastern Newspaper Society* v. *CIT* [1979] 119 ITR 996 (SC), has held that though audit objection may serve as information on the basis of which the Income-tax Officer can act, ultimate action must depend directly and solely on the formation of belief by the Income-tax Officer on his own where such information is passed on to him by the Audit Department that income has escaped assessment.

20 In the present case, from the audit para it emerges that upon the audit department bringing the above two issues to the notice of the Assessing Officer, the Assessing Officer did not agree with the objections raised by the audit department and expressed the opinion that the original assessment was not erroneous. However, it appears that on the insistence of the audit department, which found that the reply of the Assessing Officer was not tenable, the respondent-Assessing Officer has reopened the assessment. In the aforesaid premises, it is evident that the Assessing Officer did not form the requisite belief that income chargeable to tax has escaped assessment, but the reasons have been recorded on the basis of borrowed satisfaction of the audit department and not that of the Assessing Officer. Therefore, the basic requirement for assumption of jurisdiction under section 147 of the Act, namely, the formation of belief on the part of the Assessing Officer that income chargeable to tax has escaped assessment, is not satisfied in the present case. The assumption of jurisdiction by the Assessing Officer under section 147 of the Act is, therefore, invalid. The impugned notice under section 148 of the Act, therefore, cannot be sustained.

21 For the foregoing reasons, the petition succeeds and is, accordingly, allowed. The impugned notice dated March 23, 2018 issued by the respondent under section 148 of the Act for the assessment year 2012-13 is hereby quashed and set aside. Rule is made absolute accordingly, with no order as to costs.

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[2020] 425 ITR 115 (Bom)

[IN THE BOMBAY HIGH COURT — PANAJI BENCH]

BRAGANZA CONSTRUCTION PVT. LTD.

v.

ASSISTANT COMMISSIONER OF INCOME-TAX

M. S. SONAK and **C. V. BHADANG** JJ.

December 6, 2019.

SS ▸ ITA 1961, ss 69C, 254, 260A ; IT(AT)R 1963, r 29
HF ▸ Remanded

APPEAL TO APPELLATE TRIBUNAL—POWER TO PERMIT PRODUCTION OF ADDITIONAL EVIDENCE—TRIBUNAL NOT CONSIDERING APPLICATION OF ASSESSEE SEEKING LEAVE TO PRODUCE ADDITIONAL DOCUMENT AS EVIDENCE—FAILURE BY TRIBUNAL TO EXERCISE JURISDICTION VESTED IN IT—MATTER REMANDED TO TRIBUNAL—INCOME-TAX ACT, 1961, ss. 69C, 254, 260A—INCOME-TAX (APPELLATE TRIBUNAL) RULES, 1963, r. 29.

Rule 29 of the Income-tax (Appellate Tribunal) Rules, 1963 makes it clear that the Appellate Tribunal has the power to permit production of additional evidence before it if a case for production of additional evidence is made out by the parties. This means that the Tribunal is duty bound to consider the application seeking leave to produce additional evidence at the appellate stage.

Held accordingly, *that the Tribunal had not considered the assessee's application seeking leave to produce additional evidence at the stage of appeal by it. This amounted to failure to exercise jurisdiction which was vested in the Tribunal by virtue of the provisions in rule 29 of the 1963 Rules. Upon exercise of such jurisdiction, thereafter, it was open to the Tribunal to examine whether the application made by the assessee fulfilled the parameters of rule 29 of the Rules, 1963 or whether something was required to be said as regards the documents that were sought to be produced at the appellate stage. There was no discussion on whether such material could be admitted in evidence at the appellate stage and thereafter considered. The order of the Tribunal was to be set aside and the matter was to be remanded to the Tribunal for consideration of the assessee's application seeking leave to produce additional evidence before the Tribunal. [Matter remanded.]*

Tax Appeal No. 47 of 2012.

S. R. Rivankar and *Rama Rivankar*, Advocates, for the appellant.

Ms. Susan Linhares, Standing Counsel, for the respondent.

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JUDGMENT[1]

The judgment of the court was delivered by

1 M. S. SONAK J.—Heard Mr. Rivankar, the learned counsel for the appellant and Ms. Susan Linhares, the learned standing counsel for the respondent.

2 By order dated August 22, 2012, this appeal was admitted on the following substantial questions of law :

> "(i) Whether on the facts and in the circumstances of the case the Income-tax Appellate Tribunal was justified in holding that the said amount of Rs. 80 lakhs is deemed to be unexplained expenditure under the proviso to section 69C of the Income-tax Act, 1961 without considering the evidence/material placed on record by the assessee, justifying that the said amount was expended by the assessee from the bank account ?
>
> (ii) Whether the Income-tax Appellate Tribunal has exceeded its jurisdiction by treating the said amount of Rs. 80 lakhs under section 69C of the Act, when it was not the case spelt out by the Assessing Officer in the show-cause notice issued under section 147 read with section 148 of the Act ?"

3 After having heard the learned counsel for the parties, we are satisfied that yet another substantial question of law is involved in this appeal. The same, according to us, ought to read as follows :

> "(iii) Whether the Income-tax Appellate Tribunal in the facts and circumstances of the present case, was required to consider the application for production on record mere additional evidence by the appellant in the form of cheques/demand drafts and other banking documents in order to evidence the source of payments to the extent of approximately Rs. 39 lakhs, having regard to the provisions of rule 29 of the Income-tax (Appellate Tribunal) Rules, 1963 ?"

4 The issue involved in the present appeal relates to deemed unexplained expenditure under the proviso to section 69C of the Income-tax Act, 1961, (IT Act, for short). The Income-tax Appellate Tribunal in the impugned judgment and order has held that an amount of Rs. 80 lakhs expended by the appellant was required to be treated as unexplained expenditure and, consequently, deemed income of the appellant-assessee. In the appeal before the Income-tax Appellate Tribunal, the appellant has produced on record certain documents by its application dated May 3, 2011. The documents, inter alia, include reference to certain cheques, which, Mr. Rivankar,

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the learned counsel for the appellant, explains as the source of the amount and the source of the expenditure. Along with the application, even agreement dated March 30, 2004 is produced.

5 From the impugned judgment and order, we find that all this material has not even been considered. In particular, there is no discussion on whether such material could be admitted in evidence at the appellate stage or not and thereafter considered. Looking to the proviso to rule 29 of the Income-tax (Appellate Tribunal) Rules, 1963, we are satisfied that the aforesaid substantial question of law is indeed involved in this matter and is required to be decided. Further, we are satisfied that if the aforesaid substantial question of law, which we have now framed, is decided in favour of the appellant and against the Revenue, then, the matter will have to be remanded to the Income-tax Appellate Tribunal and there will be no occasion to decide the two substantial questions of law framed at the time of admission of this appeal.

6 Ms. Linhares, the learned standing counsel for the respondent, has made her submissions on the aforesaid substantial question of law, without seeking any adjournment.

7 Ms. Linhares, the learned standing counsel submits that the documents which the appellant seeks to produce before the Income-tax Appellate Tribunal, were very much available at the stage when the assessment was made. However, the same were not produced before the assessing authority. She submits that all this casts a doubt upon such evidence. She also submits that the application made by the appellant does not satisfy the predicates of rule 29 of the Income-tax (Appellate Tribunal) Rules, 1963.

8 According to us, at this stage, we are really not required to go into the issue as to whether the production of such additional evidence was to be allowed or not. From the impugned judgment and order, what we find is that the Income-tax Appellate Tribunal has not even considered the appellant's application seeking leave to produce additional evidence at the stage of appeal by it. This, according to us, amounts to failure to exercise jurisdiction, which, by virtue of the provisions of rule 29 of the Income-tax (Appellate Tribunal) Rules, 1963, was undoubtedly vested in the Income-tax Appellate Tribunal. Upon exercise of such jurisdiction, thereafter, it is open to the Income-tax Appellate Tribunal to examine whether the application made by the appellant indeed fulfils the parameters of rule 29 of the Income-tax (Appellate Tribunal) Rules, 1963 or whether something is required to be said as regards the documents that are sought to be produced at the appellate stage. However, consideration of this application was required and since the same has not been done, the impugned

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judgment and order of the Income-tax Appellate Tribunal is required to be set aside and the matter remanded to the Income-tax Appellate Tribunal for consideration of the appellant's application seeking leave to produce additional evidence before the Income-tax Appellate Tribunal.

9 In the aforesaid regard, reference is required to be made to the provisions of rule 29 of the Income-tax (Appellate Tribunal) Rules, 1963, which reads as follows :

> "*Rule 29.*—The parties to the appeal shall not be entitled to produce additional evidence either oral or documentary before the Tribunal, but if the Tribunal requires any documents to be produced or any witness to be examined or any affidavit to be filed to enable it to pass orders or for any other substantial cause, or, if the Income-tax authorities have decided the case without giving sufficient opportunity to the assessee to adduce evidence either on points specified by them or not specified by them, the Tribunal, for reasons to be recorded, may allow such document to be produced or witness to be examined or affidavit to be filed or may allow such evidence to be adduced."

10 From the aforesaid rule, it is quite clear that the Income-tax Appellate Tribunal does have the power to permit production of additional evidence before the Tribunal if the case for the same is indeed made out by the parties. This means that the Tribunal is duty bound to consider the application seeking leave to produce additional evidence at the appellate stage. Since this has not been done, the substantial question of law, now framed, is required to be answered in favour of the appellant and against the Revenue.

11 Accordingly, without going into the merits of the main matter or without even going into the merits of the application made by the appellant seeking leave to produce additional evidence at the appellate stage, we, for the aforesaid reasons, set aside the impugned judgment and order by the Income-tax Appellate Tribunal and remand I. T. A. No. 03/PNJ/2011 to the file of the Income-tax Appellate Tribunal, Panaji, for fresh adjudication. We direct that the Income-tax Appellate Tribunal considers the appellant's application seeking leave to produce additional document, in accordance with law and on its own merits. All the contentions of all the parties are specifically kept open.

12 Needless to add, that the Income-tax Appellate Tribunal shall afford opportunity of hearing to both the parties and only thereafter decide the appeal which we have now remanded to it. This appeal is accordingly disposed of in the aforesaid terms.

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There shall be no order as to costs. **13**

The parties are directed to appear before the Income-tax Appellate Tribunal/its Registry on January 10, 2020 and produce authenticated copy of this order. **14**

All concerned to act on the basis of the authenticated copy of this order. **15**

[2020] 425 ITR 119 (Guj)

[IN THE GUJARAT HIGH COURT]

PRINCIPAL COMMISSIONER OF INCOME-TAX

v.

MOHAN BHAGWATPRASAD AGRAWAL

J. B. PARDIWALA and **BHARGAV D. KARIA** JJ.

January 20, 2020.

SS ▸ ITA 1961, s 2(22)(e)
AY ▸ 2015-16
HF ▸ Assessee

DIVIDEND—DEEMED DIVIDEND—LOAN TO SHAREHOLDER—EXCEPTIONS—FINDING BY TRIBUNAL THAT MONEY LENDING FORMED SUBSTANTIAL PART OF BUSINESS OF COMPANIES—LOAN NOT ASSESSABLE AS DEEMED DIVIDEND—INCOME-TAX ACT, 1961, s. 2(22)(e).

The Assessing Officer treated the loan and advances obtained by the assessee from two companies in which the public were not substantially interested as deemed dividend under section 2(22)(e) of the Income-tax Act, 1961 as the assessee held 11.61 per cent. and 22.81 per cent., respectively, of the shareholding in these companies. The Assessing Officer rejected the assessee's contention that the two companies were covered by the specific exemption given in sub-clause (ii) of section 2(22)(e) since according to the memorandum of association of both companies, money lending was authorised on the ground that the main object of the companies was to carry on business of construction. The Commissioner (Appeals) dismissed the appeal filed by the assessee. The Tribunal found that according to the audit report of the first company for the assessment year 2014-15 its money lending business constituted a substantial part of its business as the percentage ratio of loans and advances to total funds available was 79.37 per cent., that the percentage of loan and advances to the total assets was 69.71 per cent. and that the loans and advances given to unsecured loans was at 105.25 per cent. The Tribunal found that in respect of the second company, its percentage ratio of loans and

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advances to total funds available was 35.66 per cent., that the percentage of loans and advances to total assets was 32.45 per cent. and that the ratio of loans and advances given to unsecured loans was at 56.29 per cent. The Tribunal held that though the memorandum of association of the two companies did not authorise money lending business as main object, certain paragraphs of the articles of association authorised the lending of surplus money by these companies. On appeal :

Held, *dismissing the appeal, that the Tribunal had rightly held that no addition could be made by way of deemed dividend to the income of the assessee. Although the assessee held more than 10 per cent. of the shares in the creditor companies, section 2(22)(e) did not include any advances or loans to a shareholder by the company in the ordinary course of business where lending of money was substantial business of the company. It was not disputed that both the creditor companies had money lending as the substantial part of their business. No question of law arose.*

Cases referred to :

CIT *v.* Bharat Hotels Ltd. [2019] 410 ITR 417 (Delhi) (para 5)

CIT *v.* Parle Plastics Ltd. [2011] 332 ITR 63 (Bom) (para 5)

Guruswamy (K. N.) *v.* State of Mysore [1954] AIR 1954 SC 592 (para 5)

Pradip Kumar Malhotra *v.* CIT [2011] 338 ITR 538 (Cal) (paras 5, 6)

R/Tax Appeal No. 811 of 2019.

Mrs. Mauna M. Bhatt for the appellant.

JUDGMENT[1]

The judgment of the court was delivered by

1 BHARGAV D. KARIA J.—This tax appeal under section 260A of the Income-tax Act, 1961 (hereinafter referred to as "the Act, 1961") is at the instance of the Revenue and is directed against the order dated April 12, 2019 passed by the Income-tax Appellate Tribunal, Bench "A", Ahmedabad (for short "the Tribunal") in I. T. A. No. 29/Ahd/2019 for the assessment year 2015-16.

2 The Revenue has proposed the following questions as the substantial questions of law :

> "(A) Whether on facts of the case and in law, the Appellate Tribunal is correct to hold that the assessee has received the sum of Rs. 2,50,80,923 from M/s. Shreem Design Infrastructure Pvt. Ltd.

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and Rs. 76,53,711 from M/s. Aatrey Infrastructure Pvt. Ltd. in the ordinary course of business of creditor companies ?

(B) Whether on facts of the case and in law, the Appellate Tribunal is correct to hold that provisions of section 2(22)(e) of the Act are not attracted in this case ?

(C) Whether on facts of the case and in law, the Appellate Tribunal is correct to hold that the creditor companies in this case, i.e., M/s. Shreem Design and Infrastructure Pvt. Ltd. and M/s. Aatrey Infrastructure Pvt. Ltd. are also into the business of money lending ?"

3 The Assessing Officer made a disallowance as deemed dividend under section 2(22)(e) of the Act, 1961 as the assessee was having 11.61 per cent. of shareholding in M/s. Shreem Design and Infrastructure Pvt. Ltd. (for short "SDIPL") and 22.81 per cent. shareholding in M/s. Aatrey Infrastrucutre Pvt. Ltd. (for short "AIPL"), the companies in which public are not substantially interested. The Assessing Officer, therefore, held that the provisions of section 2(22)(e) of the Act, 1961 are applicable in the case of the present assessee as the assessee has obtained loan and advances from the aforesaid companies.

4 In response to the same, the assessee filed its reply in writing stating that SDIPL and AIPL are covered by the specific exemption given in sub-clause (ii) of section 2(22)(e) of the Act which provides that any advances or loan made to a shareholder (or the said concern) by a company in the ordinary course of its business where the lending of money is a substantial part of business of the company would be excluded. It was further submitted by the assessee that at page No. 2, para-6 and at page No. 4, para-20 of the memorandum of association of both the companies, money lending was authorised. However, as the main object of both the companies was to carry on business of the builder, masons and general construction, industrial construction etc., and to carry out the construction business of property lands, flats, houses, shops, offices, industrial estate etc., the Assessing Officer made addition of Rs. 2,50,80,923 in respect of SDIPL and Rs. 76,53,711 in respect of AIPL to the extent of accumulated profit treating the same to be the deemed dividend. Thereafter the same was added to the total income of both the assessees. The appeal filed by the respondent-assessee before the Commissioner of Income-tax (Appeals) was dismissed.

5 Being dissatisfied, the assessee preferred an appeal before the Income-tax Appellate Tribunal. The Tribunal, after taking into consideration var-

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ious decisions relied upon by the assessee, arrived at the following findings :

> "12. We have heard the rival submissions and perused the material available on record. We find that the Assessing Officer has made addition on account of loans and advances taken from M/s. SDIPL and M/s. AIPL being Rs. 2,50,80,923 and Rs. 76,53,711 respectively being accumulated profit as the conditions laid down under section 2(22)(e) are satisfied. The claim of the assessee that the loans and advances were obtained in the ordinary course of business of money lending on which interest was paid at the market rate at 9 per cent. and the money lender company's substantial part of the money lending business was not accepted on the ground that the main object of the lender companies was not carrying on money lending business. The perusal of audit report for the assessment year 2014-15 shows that SDIPL has done money lending business which constitutes substantial part of its business as the percentage ratio of the loans and advances to the total funds available comes to 79.37 per cent. and the percentage of loans and advances to the total assets of the company comes to 69.71 per cent. The ratio of the loans and advances given to the unsecured loans was at 105.25 per cent. Similarly, AIPL's percentage ratio of loans and advances to the total funds available comes to 35.66 per cent. and the percentage of loans and advances to the total assets of the company comes to 32.45 per cent. The ratio of the loans and advances given to the unsecured loans was at 56.29 per cent. We further observe that though the memorandum and articles of association of the company does not authorise money lending business as main object, but page 2, para 6 and at page 4, para 20 authorised the lending of surplus money by these companies. The perusal of sub-clause (ii) of section 2(22)(e) shows that it does not envisage such a condition of authorization. In order to appreciate that there is no requirement of main object as of money lending business, it would be relevant to reproduce the sub-clause (ii) of section 2(22)(e) which reads as under :
>
> 'Any advance or loan made to a shareholder or the said concern by a company in the ordinary course of its business, where the lending of money is substantial part of business of the company.' (bold letter emphasized by us).
>
> Thus, the provision makes it clear that there is no specific requirement that memorandum of association of company specifically mentions in main object as money lending business and it is not

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necessary for licence. Now coming to the term substantial part of the company business, which has not been defined specifically, but same can be understood from *Explanation 3(b)* to section 2(22)(e) which is as follows :

'*Explanation 3(b)*—a person shall be deemed to have a substantial interest in a concern, other than a company, if he is, at any time during the previous year, beneficially entitled to not less than twenty percent. of the income of such concern.' Similar, definition is given in section 2(32) of the Act which reads as under :

'A person who has a substantial interest in the company' in relation to a company, means a person who is the beneficial owner of shares, not being shares entitled to a fixed rate of dividend whether with or without a right to participate in profits, carrying not less than twenty per cent. of the voting power'. Thus, as per definition as given in the above sections, the word used as "substantial" would mean where the assessee-company has carried on money lending business of more than 20 per cent. or more of the total income of the closely held company and turnover of loans, funds to the total fund of the company is above 20 per cent., then any loans or advances made by the said company to its shareholders cannot be deemed dividend as per the exclusion sub-clause (ii) to section 2(22)(e) of the Act. The learned counsel for the assessee supported his view by placing reliance on the decision of the hon'ble Supreme Court in the case *K. N. Guruswamy* v. *State of Mysore* [1954] AIR 1954 SC 592 and contended that the word appearing in the section and rules must be given the same meaning unless there is nothing to indicate the contrary. Since, SDIPL has carried out money lending business in the percentage ratio of the loans and advances to the total funds available comes to 79.37 per cent. and the percentage of loans and advances M/s. AIPL has carried out its money lending business in the percentage ratio of 35.65 per cent. of the loans and advances of the total funds available, which is more than twenty per cent. as mentioned in *Explanation (b)* to section 2(22)(e) and section 2(32) of the Act. Further, the hon'ble Bombay High Court in the case of *CIT* v. *Parle Plastics Ltd.* [2011] 332 ITR 63 (Bom) held as follows (at pages 74, 75) :

'Applying these tests to the present case, we do not find that the Income-tax Appellate Tribunal has committed any error in coming to the conclusion that lending of money was a substantial part of the business of AMPL. The Income-tax Appellate Tribunal has noted

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that 42 per cent. of the total assets of AMPL as on March 31, 1996 and 39 per cent. of the total assets of AMPL as on March 31, 1997 were deployed by it by way of total loans and advances. By no means, the deployment of about 40 per cent. of the total assets into the business of lending could be regarded as an insignificant part of the business of AMPL. The Income-tax Appellate Tribunal has also held that the income AMPL had received by way of interest of Rs. 1,08,18,036 while its total profit was Rs. 67,56,335. Excluding the income earned by AMPL by way of interest, the other business had resulted into net loss. In our view, the Income-tax Appellate Tribunal has taken into consideration the relevant factors and has applied the correct tests to come to the conclusion that lending of money was a substantial part of the business of AMPL. Since lending of money was a substantial part of the business of AMPL, the money given by it by way of advance or loan to the assessee could not be regarded as a dividend, as it has to be excluded from the definition of "dividend" by virtue of sub-clause (ii) of section 2(22)(e) of the Act. Hence, question No. 2 is answered in favour of the assessee and against the Revenue.'

13. In the present case, we observe that 69.71 per cent. of the total assets of SDIPL as on March 31, 2015 and 32.45 per cent. of the total assets of AIPL as on March 31, 2015 were deployed by the above lender companies by way of total loans and advances. By no means, the deployment of about 69.71 per cent. and 32.45 per cent. of the total assets into the business of lending could be regarded as an insignificant part of the business of SDIPL and AIPL. We find that SDIPL had received by way of interest of Rs. 1,67,16,067 while its total profit was Rs. 50,48,266 excluding interest income earned by SDIPL by way of interest. Similarly AIPL has earned interest income of Rs. 17,68,467 and other business had resulted into insignificant income. Therefore, we are of the considered opinion that considering the relevant factors and as ratio laid down by the hon'ble Bombay High Court in the above cited decision, the lending of money was substantial part of the business of both the lender companies under consideration from whom the assessee has received loans and advances. The learned counsel for the assessee has relied on the decision of the hon'ble Delhi High Court in the case of *CIT* v. *Bharat Hotels Ltd.* [2019] 410 ITR 417 (Delhi) ; [2019] 103 taxmann.com 295 (Delhi) wherein it was held that where the assessee received loan from two companies which were substantially involved in money lending business, the Tribunal rightly concluded that sub-clause (ii) to section 2(22)(e) would

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apply to the assessee's case and the addition of deemed dividend made to the assessee's income was to be deleted. Since lending of money was a substantial part of the business of SDIPL and AIPL, the money given by it by way of advance or loan to the assessee could not be regarded as a dividend, as it has to be excluded from the definition of 'dividend' by virtue of sub-clause (ii) to section 2(22)(e) of the Act. We therefore, hold accordingly.

14. We further find that the loan taken from the SDIPL and AIPL were compensated by way of interest at 9 per cent. being market rate paid by the assessee on loan, therefore, the assessee in real sense did not derive any benefit from the company so as to the provisions of sub-clause (ii) of section 2(22)(e) of the Act. The learned counsel for the assessee relied on the case of *Asst. CIT* v. *Zenon (India) Pvt. Ltd.* I. T. A. No. 1124/Kol/2012 (paper book 38 to 43) and *Mrs. Sangita Jain* v. *ITO* I. T. A. No. 1817/Kol/2009 (paper book 44 to 51) which supports his contentions. The learned counsel for the assessee placed reliance in the case of *Pradip Kumar Malhotra* v. *CIT* [2011] 338 ITR 538 (Cal) I. T. A. No. 219 of 2013, dated August 2, 2011 of the hon'ble Calcutta High Court (paper book 24 to 37), wherein it was held by the honourable Calcutta High Court that the phrase "by way of advance or loan" appearing in section 2(22)(e) must be construed to mean those advances or loans, which the shareholder enjoys simply on account of being a partner, who is the beneficial owner of shares, but if such loan or advance is given to such shareholder as a consequence of any further consideration, which is beneficial to the company, received from such shareholder, in such a case, such advance or loan cannot be said to be deemed dividend within the meaning of the Act. It was held that the gratuitous loan or advance given by a company to those classes of shareholders thus, would come within the purview of section 2(22)(e) but not the cases where the loan or advance is given in return to an advantage conferred upon the company by such shareholder. Since, the assessee has paid interest on loans and advances taken from SDIPL and AIPL, hence, he has compensated and no benefit has been derived. Therefore, applying the ratio of the hon'ble Calcutta High Court as quoted above, and Co-ordinate Bench decisions in *Asst. CIT* v. *Zenon (India) Pvt. Ltd.* I. T. A. No. 1124/Kol/2012 (paper book 38 to 43) and *Mrs. Sangita Jain* v. *ITO* I. T. A. No. 1817/Kol/2009 (paper book 44 to 51), the loans and advances taken by the assessee are not covered by the provisions of section 2(22)(e) of the Act. Thus, considering the totality of the facts and

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judicial decision as discussed above, we hold that the Assessing Officer was not justified in making addition on account of deemed dividend of Rs. 2,50,80,923 from SDIPL and Rs. 76,53,711 from AIPL. Hence, the same are directed to be deleted. Accordingly, the grounds of appeal raised by the assessee are allowed."

6 Thus, the Tribunal has arrived at a finding of fact that 69.71 per cent. of the total assets of SDIPL as on March 31, 2015 and 32.45 per cent. of the total assets of AIPL as on March 31, 2015 were deployed by both the companies by way of loans and advances which could not be regarded as an insignificant part of the business. The Tribunal found that SDIPL had received, by way of interest, a sum of Rs. 1,67,16,067 against its total profit of Rs. 50,48,266 excluding the income earned by SDIPL by way of interest. Similarly AIPL has earned an amount of Rs. 17,68,467 by way of interest and other business which resulted into insignificant income. The Tribunal also recorded that both the companies were paid the interest on the loan and advances obtained by them at the market rate of 9 per cent. The Tribunal, has also taken into consideration the decision of the Calcutta High Court in the case of *Pradip Kumar Malhotra* v. *CIT* [2011] 338 ITR 538 (Cal) I. T. A. No. 219 of 2013, dated August 2, 2011, which was relied upon by the assessee, wherein it has been held that the phrase "by way of advance or loan" appearing in section 2(22)(e) must be construed to mean those advances or loans, which the shareholder enjoys for simply on account of being a partner, who is the beneficial owner of shares, but if such loan or advance is given to such shareholder as a consequence of any further consideration, which is beneficial to the company, received from such shareholder, in such a case, such advance or loan cannot be said to be deemed dividend within the meaning of section 2(22)(e) the Act.

7 It would be, therefore, germane to refer to the provisions of section 2(22)(e) of the Act, 1961, which reads thus :

"2(22)(e) : any payment by a company, not being a company in which the public are substantially interested, of any sum (whether as representing a part of the assets of the company or otherwise) made after the 31st day of May, 1987, by way of advance or loan to a shareholder, being a person who is the beneficial owner of shares (not being shares entitled to a fixed rate of dividend whether with or without a right to participate in profits) holding not less than ten per cent of the voting power, or to any concern, in which such shareholder is a member or a partner and in which he has a substantial interest (hereafter in this clause referred to as the said concern) or any payment by any such company on behalf, or for the individual benefit, of any such

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shareholder, to the extent to which the company in either case possesses accumulated profits ;

but "dividend" does not include—

(i) a distribution made in accordance with sub-clause (c) or sub-clause (d) in respect of any share issued for full cash consideration, where the holder of the share is not entitled in the event of liquidation to participate in the surplus assets ;

(ia) a distribution made in accordance with sub-clause (c) or sub-clause (d) in so far as such distribution is attributable to the capitalised profits of the company representing bonus shares allotted to its equity shareholders after the 31st day of March, 1964, and before the 1st day of April, 1965 ;

(ii) any advance or loan made to a shareholder or the said concern by a company in the ordinary course of its business, where the lending of money is a substantial part of the business of the company ;

(iii) any dividend paid by a company which is set off by the company against the whole or any part of any sum previously paid by it and treated as a dividend within the meaning of sub-clause (e), to the extent to which it is so set off.

Explanation 1.—The expression 'accumulated profits', wherever it occurs in this clause, shall not include capital gains arising before the 1st day of April, 1946, or after the 31st day of March, 1948, and before the 1st day of April, 1956 ;

Explanation 2.—The expression 'accumulated profits' in sub-clauses (a), (b), (d) and (e), shall include all profits of the company up to the date of distribution or payment referred to in those sub-clauses, and in sub-clause (c) shall include all profits of the company up to the date of liquidation, but shall not, where the liquidation is consequent on the compulsory acquisition of its undertaking by the Government or a corporation owned or controlled by the Government under any law for the time being in force, include any profits of the company prior to three successive previous years immediately preceding the previous year in which such acquisition took place.

Explanation 3.—For the purposes of this clause,—

(a) 'concern' means a Hindu undivided family, or a firm or an association of persons or a body of individuals or a company ;

(b) a person shall be deemed to have a substantial interest in a concern, other than a company, if he is, at any time during the previous year, beneficially entitled to not less than twenty per cent. of the income of such concern ;"

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8 On perusal of the above provision, it is clear that as the assessee was holding more than 10 per cent. of the shares in both the companies, the provisions of section 2(22)(e) of the Act would come into play. However, the section further provides that the dividend does not include any advances or loan made to a shareholder by the company in the ordinary course of business where lending of money is a substantial part of the business of the company. In the case on hand, it is not in dispute that both the companies were having money lending as the substantial part of their business. Therefore, the Tribunal has rightly held that no addition can be made by way of deemed dividend in the case of the assessee.

9 In view of the above, no question of law, much less any substantial question of law would arise for the determination of this court. The appeal stands dismissed accordingly.

[2020] 425 ITR 128 (Ker)

[IN THE KERALA HIGH COURT]

FCI OEN CONNECTORS LTD.

v.

DEPUTY COMMISSIONER OF INCOME-TAX AND ANOTHER

A. K. JAYASANKARAN NAMBIAR J.

November 13, 2019.

SS ▸ ITA 1961, s 144C(2)
AY ▸ 2015-16
HF ▸ Assessee

DRAFT ASSESSMENT ORDER—LIMITATION FOR FILING OBJECTIONS BEFORE DISPUTE RESOLUTION PANEL—DRAFT ASSESSMENT ORDER SERVED THROUGH ELECTRONIC MODE ON AN EARLIER DATE BUT ASSESSEE OPTING FOR MANUAL PROCEEDINGS—LIMITATION TO BE CALCULATED FROM DATE OF RECEIPT OF DRAFT ASSESSMENT ORDER MANUALLY BY ASSESSEE—INCOME-TAX ACT, 1961, s. 144C(2).

In the event of an ambiguity in construing the provisions in a taxing statute, the court has to take a view that favours the assessee.

For the assessment year 2015-16, the assessee was served with notices under sections 143(2) and 142(1) of the Income-tax Act, 1961 requiring it to produce various documents in connection with the completion of its assessment. With effect from the year 2017, as part of the Government initiative towards e-governance, there was a move to shift to e-proceedings facility for

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completion of assessments. For the assessees who did not want to opt for the e-proceeding facility, the Department permitted a continuation of the manual procedure for completion of the assessments. Therefore, the assessee, in response to the notices received manually filed the documents sought for by the Department. On a reference to the Transfer Pricing Officer under section 92CA, he recommended certain adjustments to the computation of income, in accordance with the transfer pricing norms. Thereafter, the Assessing Officer based on the recommendations of the Transfer Pricing Officer served a copy of the draft assessment order under section 144C to the assessee electronically on December 31, 2018 and manually on January 5, 2019. According to the provisions of section 144C(2) the assessee had to file his objections to the draft assessment order, before the Dispute Resolution Panel, within 30 days of receipt of the draft order by him. The objection filed by the assessee was received by the Dispute Resolution Panel on February 1, 2019. The Panel issued a notice, asking the assessee to show cause why the objection preferred by it should not be rejected on the ground that it was received by the Panel more than 30 days after the service of the draft assessment order through the electronic mode on December 31, 2018. In response to the show-cause notice, the assessee submitted that the draft assessment order was manually served only on January 5, 2019 and hence its objection filed on February 1, 2019 had to be seen as within the permitted time limit of 30 days from the date of service of the draft assessment order. This contention was rejected by the Panel by an order dated February 26, 2019. Before this on February 22, 2019 itself, the assessing authority passed an assessment order without taking note of the objection filed by the assessee to the draft assessment order. On a writ petition:

Held, *allowing the petition, that when the assessee had not opted for the e-proceeding facility, and had chosen to have its assessment proceedings continued in the manual mode, the date of receipt of the draft assessment order in the manual mode had to be seen as the date of service of the draft assessment order. It was the receipt of the draft assessment order on January 5, 2019 through the manual mode, that determined the starting point of limitation for the period of 30 days under section 144C(2) for the assessee to have submitted his objections before the Dispute Resolution Panel. Reckoning the period of 30 days from January 5, 2019 the objection filed by the assessee on February 1, 2019 before the Panel was within time and its order was to be set aside. The order of assessment that did not await the decision of the Panel on the merits was also illegal.*

W. P. (C). No. 11952 of 2019 (T).

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Joseph Markose, Senior Counsel, *V. Abraham Markos*, *Abraham Joseph Markos*, *Isaac Thomas*, *P. G. Chandapillai Abraham*, *Vipin Anto H. M.*, *Alexander Joseph Markos* and *Sharad Joseph Kodanthara* for the petitioner.

Jose Joseph, Standing Counsel, for the respondents.

JUDGMENT

1 A. K. JAYASANKARAN NAMBIAR J.—The petitioner is a public limited company engaged in the business of manufacture of connectors and other articles. It is an assessee under the Income-tax Act on the files of the first respondent. For the assessment year 2015-16, the petitioner filed its returns and as part of the assessment procedure, it was served with a section 143(2) notice on April 15, 2016. Thereafter, it was served with various notices under section 142(1) of the Income-tax Act, 1961 requiring it to produce various documents in connection with the completion of its assessment. It is relevant to note at this stage that, with effect from 2017, as part of the Government initiative towards e-Governance, there was a move to shift to e-proceedings facility for completion of assessments. Circulars and instructions were therefore issued by the Government of India, Ministry of Finance, in the Department of Revenue, requesting the assessees to switch over to the e-proceedings facility available on the integrated platform provided through the income-tax business application project, for completion of their assessments under the Income-tax Act.

2 The e-proceeding facility was introduced initially in seven metro cities, where the said facility was made mandatory for the assessees. In Cochin, the e-proceeding facility was permitted as an optional facility for those assessees who wanted to opt for the said facility. For others like the petitioner herein, who did not want to opt for the e-proceeding facility, the Department permitted a continuation of the manual procedure for completion of the assessments. It is therefore that the petitioner, in response to the notices received by him under section 142(1) of the Income-tax Act, manually filed the documents sought for by the Department through exhibits P5, P7 and P12 communications dated October 9, 2017, September 12, 2018 and December 28, 2018 respectively. It would appear that, on a reference to the Transfer Pricing Officer under section 92CA of the Income-tax Act, the said Officer by order dated October 26, 2018 recommended certain adjustments to the computation of income, in accordance with the transfer pricing norms. Thereafter, the Assessing Officer prepared a draft assessment order based on the recommendations of the Transfer Pricing Officer, in terms of section 144C of the Act and served a copy of the

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draft assessment order to the petitioner electronically on December 31, 2018 and manually on January 5, 2019.

3 As per the provisions of sub-section (2) of section 144C, the petitioner had to file his objections to the draft assessment order, before the Dispute Resolution Panel, within 30 days of receipt by him of the draft order. It is not in dispute that the objection filed by the petitioner was received by the Dispute Resolution Panel on February 1, 2019 as is evident from exhibit P16 communication. The Dispute Resolution Panel, however, issued exhibit P17 show-cause notice, asking the petitioner to show cause as to why the objection preferred by it should not be rejected on the ground that it was received by the Panel more than 30 days, after the service of the draft assessment order through the electronic mode on December 31, 2018. In response to the said show-cause notice, the petitioner-assessee informed the Dispute Resolution Panel that the draft assessment order was manually served only on January 5, 2019 and hence its objection filed on February 1, 2019 had to be seen as within the permitted time limit of 30 days from the date of service of the draft assessment order. This contention of the petitioner was however, rejected by the Dispute Resolution Panel by exhibit P19 order dated February 26, 2019. Much before this however, on February 22, 2019 itself, by exhibit P20 order, the first respondent-assessing authority passed an assessment order without taking note of the objection filed by the petitioner to the draft assessment order. This was probably on account of the fact that a copy of the objection filed by the assessee to the draft assessment order on February 1, 2019 before the Dispute Resolution Panel was received by the assessing authority only on February 5, 2019, which was beyond the period of 30 days from January 5, 2019, the date on which the draft assessment order in manual mode was served on the petitioner-assessee. In the writ petition, exhibit P19 order of the Dispute Resolution Panel, and exhibit P20 order of assessment are impugned, inter alia, on the contention that the Dispute Resolution Panel, as well as the assessing authority, ought to have considered the objections filed by the petitioner to the draft assessment order before completing the assessment of the petitioner under the Act.

4 A statement has been filed on behalf of the respondent wherein, the stand taken is that, inasmuch as the draft assessment order in electronic format was served on the petitioner-assessee on December 31, 2018/January 1, 2019, the petitioner-assessee had to file its objection before the Dispute Resolution Panel by February 1, 2019. It is therefore contended that, since the objections of the assessee were admittedly filed only on February 5, 2019, the same was belated vis-a-vis the Dispute Resolution Panel, as also

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the Assessing Officer and hence exhibits P19 and P20 orders cannot be seen as vitiated on account of any procedural error occasioned by the respondent.

5 I have heard the learned senior counsel Sri Joseph Markose appearing for the petitioner and also Sri Jose Joseph, the learned standing counsel for the Income-tax Department. On a consideration of the facts and circumstances of the case as also the submissions made across the Bar, I find that the e-proceeding facility that was introduced as part of the Government initiative towards e-Governance, in the Income-tax Department, was not made mandatory for proceedings initiated against the assessees in Kochi city. Save for the assessees in the seven metro cities specified, of which Kochi is not one, for the assessees located elsewhere in the country, the e-proceeding facility was made optional, and if the assessees chose not to opt for the electronic facility, the proceedings vis-a-vis the Department had to be conducted manually. The services of notices under section 142(1) or 143(2) and the replies/objections by the assessees had therefore, to be effected manually, although, in the absence of any objection by the assessee, an electronic service could also have been resorted to by the Department. In the instant case, the issue that arises for the consideration is whether, the service of the draft assessment order on the assessee, in terms of section 144C of the Income-tax Act, was effected on December 31, 2018/ January 1, 2019 as contended by the Department or only on January 5, 2019 as contended by the petitioner-assessee. It is not in dispute that the draft assessment order in electronic format was sent to the petitioner-assessee on December 31, 2018/January 1, 2019. The Department, however, chose to send a manual version of the draft assessment order also to the petitioner-assessee, and this was received by the petitioner on January 5, 2019. In terms of section 144C(2) of the Income-tax Act, the petition-assessee was to submit his objections to the draft assessment order within 30 days of the receipt of the same, and the said objections were to be simultaneously sent to both the Dispute Resolution Panel as also to the Assessing Officer. It is trite, that in matters involving transfer pricing, and where a reference is made to the Transfer Pricing Officer, the final assessment must await the decision of the Transfer Pricing Officer, or in applicable cases, that of the Dispute Resolution Panel. The relevant date in the instant case, which involved a reference to the Transfer Pricing Officer, has to be the date on which the objections were received by the Dispute Resolution Panel and the question to be answered is whether, the objections filed by the petitioner on February 1, 2019 was within the time as contemplated under section 144C of the Income-tax Act.

6 In my view, when the petitioner had not opted for the e-proceeding facility, and had chosen to have its assessment proceedings continued in

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the manual mode, the date of receipt of the draft assessment order in the manual mode has to be seen as the date of service of the draft assessment order. This would be so because, an assessee who did not opt for the electronic mode for the completion of his assessment proceedings, virtually expresses his lack of confidence in the said facility and thereby chooses to opt for the manual facility in which he reposes greater confidence. Till such time as the electronic facility is made mandatory for the assessees, therefore, the wishes of the assessee have necessarily to be respected by the Department. It would also be an aspect of fairness in tax administration that the assessee is not prejudiced on account of service of an order, through a mode that he did not opt for. This court must also remind itself that, in the event of an ambiguity in construing the provisions in a taxing statute, it has to take a view that favours the assessee. I am therefore of the view that it is the receipt of the draft assessment order on January 5, 2019 through the manual mode, that determines the starting point of limitation for the period of 30 days under section 144C(2) of the Income-tax Act, for the petitioner to have submitted his objections before the Dispute Resolution Panel. On reckoning the period of 30 days from January 5, 2019 as aforesaid, I find that the objection filed by the petitioner on February 1, 2019 before the Dispute Resolution Panel was within time. Exhibit P19 order of the Dispute Resolution Panel must, on that reasoning, be set aside and I do so. As already noticed, in matters involving transfer pricing, the assessment order by the Assessing Officer must necessarily follow the findings of the Dispute Resolution Panel and hence, based on the finding that exhibit P19 order of the Dispute Resolution Panel is illegal, I have to hold that exhibit P20 order of assessment, that did not await the decision of the Dispute Resolution Panel on merits, is also illegal.

The writ petition is therefore allowed by quashing exhibits P19 and P20 orders and directing the second respondent-Dispute Resolution Panel to consider the objections of the petitioner to the draft assessment order on merits, and pass fresh orders in lieu of exhibit P19 within a period of three months from the date of receipt of a copy of this judgment. The first respondent-Assessing Officer shall thereafter, complete the assessment proceedings, taking note of the order of the second respondent, and after hearing the petitioner, within a further period of three months from the date of receipt of the order of the second respondent. It is made clear that the findings in this judgment have been entered taking note of the peculiar factual circumstances that arose in the instant case, and hence this judgment is not to be cited as a precedent in subsequent cases.

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[2020] 425 ITR 134 (Bom)

[IN THE BOMBAY HIGH COURT]

PRINCIPAL COMMISSIONER OF INCOME-TAX

v.

ANTHONY JOHN PEREIRA

UJJAL BHUYAN and MILIND N. JADHAV JJ.

February 4, 2020.

SS ▶ ITA 1961, ss 2, 45
AY ▶ 2011-12
HF ▶ Assessee

CAPITAL GAINS—EXEMPTION—PROFITS FROM SALE OF AGRICULTURAL LAND—MEANING OF AGRICULTURAL LAND—CONDITIONS LAID DOWN IN SECTION 2(14) FOR TREATING AGRICULTURAL LAND AS NON-AGRICULTURAL—ONE OF THE CONDITIONS SATISFIED—LAND IN VILLAGE WITHIN MUNICIPALITY—VILLAGE HAVING POPULATION LESS THAN SPECIFIED TEN THOUSAND—LAND WAS AGRICULTURAL—PROFITS FROM SALE OF LAND ENTITLED TO EXEMPTION—INCOME-TAX ACT, 1961, SS. 2, 45.

What section 2(14)(iii)(a) of the Income-tax Act, 1961, contemplates is that capital asset does not include agricultural land. But land would not be treated as agricultural land if it is situated within the jurisdiction of a municipality or a cantonment board and which has a population of not less than 10,000. Therefore, inversely speaking, land which is outside the jurisdiction of a municipality or a cantonment board and which has a population of less than 10,000 would come within the ambit of the expression "agricultural land" to be excluded from "capital asset". The use of the word "and" between the two conditions, i. e., first condition being that it is not situated within the jurisdiction of a municipality or a cantonment board and the second being that such area having a population of not less than 10,000, to bring the land outside the purview of agricultural land, is indicative of the legislative intent that the two requirements have to be read conjunctively. In other words, both the requirements or conditions would have to be fulfilled to bring the land outside the scope and ambit of agricultural land to be treated as a capital asset. Otherwise, even if one of the requirements is not fulfilled or is not present, it would be an agricultural land which would not be included within and treated as capital asset.

Held, *dismissing the appeal, that the land which was sold was situated in a village J. Legally speaking, July 3, 2009 was the date of constitution of the larger urban area by the name of Municipal Corporation of the city of*

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Vasai-Virar of which the village J became a part. Late collection of tax by the Municipal Corporation or mentioning or recording in the revenue record that the village continued to be a separate entity till May 31, 2011 would not make any material difference to the legal position that the village became part of the larger urban area on and from July 3, 2009. However, the Tribunal returned a finding of fact that at the time of sale, the land in question was situated at village J, the population of which was 5,912 which was less than the statutory requirement of 10,000. Thus, this condition being absent the land was rightly treated as agricultural land, not included within the ambit and meaning of capital asset. The profit from sale of the land was not assessable as capital gains.

Income Tax Appeal No. 1223 of 2017.

Tejveer Singh, Standing Counsel, for the appellant.

N. M. Gandhi for the respondent.

JUDGMENT

1 Heard Mr. Tejveer Singh, learned standing counsel, Revenue for the appellant and Mr. N. M. Gandhi, learned counsel for the respondent-assessee.

2 This appeal has been filed under section 260A of the Income-tax Act, 1961 ("the Act" for short) by the Revenue against the order dated August 25, 2016 passed by the Income-tax Appellate Tribunal, "A" Bench, Mumbai ("Tribunal" for short) in Income Tax Appeal No. 1103/Mum/2016 for the assessment year 2011-12.

3 The appeal has been preferred projecting the following two questions as substantial questions of law :

> "(a) Whether on the facts and in the circumstances of the case and in law, the Tribunal is justified in holding that the land sold by the assessee was not within the jurisdiction of any municipality being an agricultural land and was not situated within 8 kms. from any municipality though the record clearly shows that the Government of Maharashtra has constituted Vasai-Virar Municipal Corporation vide Notification No. MIS 2306/412/CR-223/2006/UD-24, dated July 3, 2009 and the Tribunal is wrong in holding that Vasai-Virar Municipal Corporation is constituted by Notification No. VVM 2009/88/CR-244/09/UD-23, dated May 31, 2011 without appreciating the fact that it only amends the Notification dated July 3, 2009 ?
>
> (b) Whether on the facts and in the circumstances of the case and in law, the Tribunal is justified in not appreciating the fact that the

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assessee was engaged in sale of land and therefore, the land transaction was in the nature of trade and liable to tax ?"

4 To appreciate the questions proposed, it would be necessary to advert to the relevant facts.

5 In the assessment proceedings for the assessment year 2011-12, the Assessing Officer noted that though the assessee had disclosed 17 sale transactions pertaining to the assessment year under consideration, 3 transactions were not disclosed. The transactions took place on April 21, 2010, May 1, 2010 and August 20, 2010. After giving notice to the assessee and after hearing the assessee, the Assessing Officer in his assessment order dated March 28, 2014 took the view that the assessee was making investment in the land and was in the business of construction and land development. In response to the contention of the assessee that the lands which were sold could not be brought within the tax regime as those were agricultural lands being outside urban limits, the Assessing Officer did not accept such contention and relying upon the Government of Maharashtra Notifications dated July 3, 2009 and May 31, 2011 held that lands which were sold fell within the Municipal Corporation of Vasai-Virar and, therefore, could not be treated as agricultural land to take the same outside the purview of the Act. It was held that such lands were to be treated as "capital asset" and the profits on sale of such lands was to be included in the total income of the assessee.

6 The assessee preferred an appeal before the Commissioner of Income-tax (Appeals)-3, Thane, against the aforesaid order of assessment. By the appellate order dated January 21, 2016 the first appellate authority upheld the findings of the Assessing Officer and dismissed the appeal of the assessee.

7 Aggrieved by the same, the assessee preferred further appeal before the Tribunal. By the impugned order dated August 25, 2016 the Tribunal allowed the appeal of the assessee by holding that the land sold was agricultural land situated at village Juchandra and became urban land only on and from May 31, 2011 being part of Vasai-Virar Municipal Corporation. The Tribunal also held that the population of village Juchandra was 5,912 as per the latest census. Therefore vide the impugned order the Tribunal allowed the appeal of the assessee on the above ground.

8 Aggrieved by the above, the Revenue is in appeal before us raising the above two questions for consideration.

9 In the hearing which took place on January 27, 2020, learned standing counsel was directed to produce the Government of Maharashtra

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notifications dated September 14, 2006, July 3, 2009 and May 31, 2011 relating to constitution of Vasai-Virar Municipal Corporation.

10 In the hearing today, Mr. Singh, learned standing counsel, Revenue for the appellant has produced copies of the above three notifications.

11 The contention of Mr. Singh, learned standing counsel, Revenue is that by the notification dated July 3, 2009 issued by the Urban Development Department, Government of Maharashtra July 3, 2009 was specified as the day on which the Municipal Corporation of the city of Vasai-Virar was constituted. The Municipal Corporation of the city of Vasai-Virar comprises of Vasai Municipal Council, Navghar-Manikpur Municipal Council, Nalasopara Municipal Council, Virar Municipal Council smaller area and 53 villages in the district of Thane. He submits that on objection raised that the 53 villages should be excluded from the Municipal Corporation of the city of Vasai-Virar, the Government of Maharashtra in the Urban Development Department issued subsequent notification dated May 31, 2011 excluding 29 villages but the village of Juchandra was not excluded. Therefore, his contention is that village of Juchandra was part of the Municipal Corporation of Vasai-Virar on and from July 3, 2009. The sale of land having taken place thereafter during the assessment year 2011-12, those lands cannot be treated as agricultural lands and earnings from the sale of such land would be income from capital gains.

12 On the other hand, learned counsel for the respondent submits that questions as framed relates to finding of fact by the Tribunal and, therefore, no question of law arises therefrom. He has referred to the impugned order passed by the Tribunal as well as the provisions of section 2(14)(iii)(a) of the Act to contend that there was no error or infirmity in the view taken by the Tribunal. He submits that firstly the Tribunal was justified in holding that Juchandra village became urban land as part of Vasai-Virar Municipal Council on and from May 31, 2011 ; secondly, the Tribunal had returned a finding of fact based on official document that the population of village Juchandra was 5,912 which is less than the statutory figure of 10,000 and therefore the land situated within Juchandra village would stand excluded from the meaning of capital asset. Third contention is that even though village Juchandra became part of the Vasai-Virar Municipal Corporation on and from May 31, 2011, the said Municipal Corporation actually started functioning as a Municipal Corporation with effect from the assessment year 2012-13. Therefore, the Tribunal was fully justified in treating the sale transaction pertaining to the land in village Juchandra as sale of agricultural land and thus exempt from payment of income-tax.

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13 The submissions made by learned counsel for the parties have been considered.

14 Before adverting to the order passed by the Tribunal it would be apposite to refer to the relevant statutory provisions. Section 2 of the Act is the definition section. Clause (14) thereof defines "capital asset". Though clause (14) is quite longish, only that portion which is relevant for the present application would be referred to. Briefly stated, clause (14) defines "capital asset" to mean property of any kind held by an assessee, whether or not connected with his business or profession ; and any securities held by a foreign institutional investor which has invested in such securities in accordance with the regulations made under the Securities and Exchange Board of India Act, 1992 but does not include agricultural land in India not being land situated in any area which is comprised within the jurisdiction of a municipality by whatever name called or a Cantonment Board and which has a population of not less than 10,000. This is mentioned in sub-clause (iii)(a) of clause (14) of section 2 of the Act.

15 Therefore, what this provision, i.e., section 2(14)(iii)(a) of the Act contemplates is that capital asset does not include agricultural land. But land would not be treated as agricultural land if it is situated within the jurisdiction of a municipality or a Cantonment Board and which has a population of not less than 10,000. Therefore, inversely speaking, a land which is outside the jurisdiction of a municipality or a Cantonment Board and which has a population of less than 10,000 would come within the ambit of the expression "agricultural land" to be excluded from "capital asset". The use of the word "and" between the two conditions, i.e., the first condition being not situated within the jurisdiction of a municipality or a Cantonment Board and second being such area having a population of not less than 10,000, to bring the land outside the purview of agricultural land, is indicative of the legislative intent that the two requirements as alluded to hereinabove would have to be read conjunctively. In other words, both the requirements or conditions would have to be fulfilled to bring the land outside the scope and ambit of agricultural land to be treated as capital asset. Otherwise, even if one is not fulfilled or is not present, it would be an agricultural land which would not be included within and treated as capital asset.

16 At this stage, we may mention that learned standing counsel, Revenue had argued that the expression "any area" has to be read as synonymous with the expression municipality when such area becomes part of the municipality. On a careful reading of sub-clause (iii)(a) of section 2(14) of the Act, we are unable to agree to such contention of learned standing

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counsel. Reading the provision as a whole we are of the considered opinion that the municipality as mentioned therein is a larger area comprising of many smaller areas and the expression "any area" is a fraction of the larger area. Therefore, the expression "any area" would refer to a smaller area within the municipality. This is because the population of the municipality has to be more than the population of "any area" ; certainly more than 10,000.

17 Having discussed the legal provisions as above, we may now advert to the relevant facts.

18 There is no dispute that the Government of Maharashtra had issued draft notification on September 14, 2006 proposing to form a city having a corporation to be called Municipal Corporation of the city of Vasai-Virar. The schedule given comprised of 53 villages including the village of Juchandra at serial No. 19. After hearing the claims and objections, the Government of Maharashtra issued notification dated July 3, 2009 constituting the Municipal Corporation of the city of Vasai-Virar specifying the date of such constitution as July 3, 2009. The said corporation included the village of Juchandra as per final notification. It appears that an objection was made thereafter for excluding all the 53 villages including the village of Juchandra. After considering the matter, the Government of Maharashtra issued a notification dated May 31, 2011 excluding from the Municipal limits of Municipal Corporation of the city of Vasai-Virar 29 villages as per schedule to the said notification. However, the village in question, i.e., village of Juchandra was not included in the list of excluded villages. Therefore, it continued to remain within the Municipal Corporation of the city of Vasai-Virar.

19 We may now advert to the impugned order passed by the Tribunal. In para9 of the impugned order, the Tribunal held that the agricultural land situated at village Juchandra remained as a rural area and became urban land on and from May 31, 2011. That apart the Tribunal held that the Municipal Corporation started collecting taxes from the assessment year 2012-13 onwards. Besides, the revenue records disclosed Juchandra village as a separate entity till May 31, 2011. In this backdrop, the Tribunal concluded that the land sold by the respondent-assessee at Juchandra village was agricultural land since the sale transaction had taken place prior to May 31, 2011.

20 On this point, we cannot agree with the finding returned by the Tribunal. The Government of Maharashtra notification dated July 3, 2009 clearly mentioned that under sub-sections (2) and (2A) of section 3 of the Bombay Provincial Municipal Corporations Act, 1949, the Vasai-Virar

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Municipal Corporation was constituted and July 3, 2009 was specified to be the date when the larger urban area comprising the whole of Vasai Municipal Council, Navghar-Manikpur Municipal Council, Nalasopara Municipal Council, Virar Municipal Council smaller area and 53 villages including the village of Juchandra were declared as forming the city having a Corporation by the name of Municipal Corporation of the city of Vasai-Virar. Therefore, legally speaking, July 3, 2009 is the date of constitution of the larger urban area by the name of Municipal Corporation of the city of Vasai-Virar of which the village Juchandra became a part. It is another matter that by the subsequent notification dated May 31, 2011, 29 villages were excluded from the aforesaid urban area, but that does not mean that May 31, 2011 is the date for constitution of the Municipal Corporation. Late collection of tax by the Municipal Corporation or mentioning/recording in the revenue record that the said village continued to be a separate entity till May 31, 2011 would not make any material difference to the legal position that the village became part of the larger urban area on and from July 3, 2009.

21 Having noted that, we may once again revert back to the requirements of sub-clause (iii)(a) of clause (14) to section 2 of the Act. For land to be excluded from capital asset, it has to be agricultural land in India ; such land to be not agricultural must fulfil two conditions, viz., it must be a land situated in any area which is comprised within the jurisdiction of a municipality or Cantonment Board and which has a population of not less than 10,000. These two conditions are preconditions and must be read conjunctively. In other words, if both the conditions are present then it would not be agricultural land and would be treated as capital asset. However, inversely speaking, if either of the two conditions are absent then the land would be agricultural land and excluded from capital asset. Though we have held the land in question to be within the jurisdiction of a municipality, we find the second condition to bring the land outside the ambit of agricultural land, i. e., that the area has a population which is not less than 10,000 absent. In this connection, the Tribunal had considered the census report as well as the population certificate of the village dated June 2, 2008 and other relevant documents and thereafter returned a finding of fact that at the time of sale, the land in question was situated at village Juchandra, the population of which was 5,912 which is less than the statutory requirement of 10,000. Thus, this condition being absent the sold land was rightly treated as agricultural land, not included within the ambit and meaning of capital asset.

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This is a finding of fact which has not been questioned by the Revenue as perverse being contrary to the record as would be evident from the two questions which have been raised. On this finding of fact, we are of the opinion that the Tribunal was justified in holding that the lands which were sold were agricultural lands, not forming part of capital asset within the meaning of section 2(14) of the Act. **22**

Consequently and in the light of the above, we answer both the questions in favour of the assessee and against the Revenue. **23**

The appeal is accordingly dismissed. However, there shall be no order as to costs. **24**

[2020] 425 ITR 141 (Bom)

[IN THE BOMBAY HIGH COURT]

COMMISSIONER OF INCOME-TAX (INTERNATIONAL TAXATION)

v.

TAJ TV LTD.

UJJAL BHUYAN and MILIND N. JADHAV JJ.

February 6, 2020.

SS ▸ DTAA (Mauritius), art 5
AY ▸ 2004-05, 2005-06
HF ▸ Assessee

NON-RESIDENT—TAXABILITY IN INDIA—MEANING OF "PERMANENT ESTABLISHMENT"—COMPANY IN MAURITIUS ENGAGED IN TELECASTING SPORTS EVENTS—AGREEMENT WITH INDIAN COMPANY FOR EXHIBITION OF TELECASTS IN INDIA—FINDING THAT AGREEMENT WAS ON PRINCIPAL TO PRINCIPAL BASIS—INDIAN COMPANY DID NOT CONSTITUTE PERMANENT ESTABLISHMENT OF FOREIGN COMPANY—INCOME EARNED NOT ASSESSABLE IN INDIA—DOUBLE TAXATION AVOIDANCE AGREEMENT BETWEEN MAURITIUS AND INDIA, art. 5[1].

WORDS AND PHRASES—"PERMANENT ESTABLISHMENT"—MEANING OF.

Article 5 of the Double Taxation Avoidance Agreement was entered into between India and Mauritius defines "permanent establishment". The sum and substance of paragraph (4) of article 5 is that a person acting in a Contracting State on behalf of an enterprise of the other Contracting State shall be deemed to be a permanent establishment of that enterprise in the first-mentioned Contracting State if he habitually exercises in the first Contracting

1. [1984] 146 ITR (St.) 214.

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State an authority to conclude contracts in the name of the enterprise and habitually maintains in the first Contracting State a stock of goods or merchandise belonging to the enterprise from which he regularly fulfils orders on behalf of the enterprise.

The assessee was a company registered in Mauritius and was a tax resident of that country. The assessee was engaged in telecasting sports channel. The assessee had appointed T as its distributor to distribute the channel to cable systems for exhibition to subscribers in India. In this connection, an agreement dated March 1, 2002 was entered into between the assessee and T. The Assessing Officer held that the income earned in terms of the agreement was assessable in India. This order was reversed by the Commissioner (Appeals) on a finding of fact that T was not acting as agent of the assessee but had obtained the right of distribution of the channel for itself and subsequently, had entered into contracts with other parties in its own name in which the assessee was not a party, that the distribution of the revenue between the assessee and T was in the ratio of 60 : 40 and the entire relationship was on principal to principal basis. The Tribunal noted that this finding of the first appellate authority was corroborated by the terms and conditions of the distribution agreement as well as the sub-distributor agreement. The Tribunal held that none of the conditions as stipulated in article 5(4) of the Double Taxation Avoidance Agreement was applicable to constitute agency permanent establishment, because T was acting independently qua its distribution rights and the entire agreement was on principal to principal basis. Therefore, it held that the distribution income earned by the assessee could not be taxed in India because T did not constitute an agency permanent establishment under the terms of article 5(4) of the Double Taxation Avoidance Agreement. On appeal :

Held, *dismissing the appeal, that there was a concurrent finding of fact by the Commissioner (Appeals) and the Tribunal. There was no evidence that the finding of fact was perverse. Hence the income from distribution earned by the assessee was not taxable in India.*

Income Tax Appeal (IT) Nos. 1984 and 1437 of 2017.

Tejveer Singh, Standing Counsel, for the appellant.

Madhur Agarwal along with *Atul K. Jasani* for the respondent.

JUDGMENT

1 This order will dispose of both Income Tax Appeal Nos. 1437 and 1984 of 2017.

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2 Heard Mr. Singh, learned standing counsel Revenue for the appellant and Mr. Agarwal along with Mr. Jasani, learned counsel for the respondent.

3 Income Tax Appeal No. 1437 of 2017 has been preferred by the Revenue against the common order dated July 5, 2016 passed by the Income-tax Appellate Tribunal, Mumbai Bench "L", Mumbai (Tribunal) in I. T. A. Nos. 4176/ Mumbai/2009 and 4706/Mumbai/2009 for the assessment year 2005-06.

4 Income Tax Appeal No. 1984 of 2017 has been preferred by the Revenue against the aforesaid common order dated July 5, 2016 passed by the Tribunal in I. T. A. Nos. 412/Mumbai/2008 and 5536/Mumbai/2008 for the assessment year 2004-05.

5 However, for the sake of convenience, the facts of Income Tax Appeal No. 1984 of 2017 which pertains to earlier assessment year, i.e., the assessment year 2004-05 are being considered.

6 This appeal has been preferred by the Revenue under section 260A of the Income-tax Act, 1961 (briefly "the Act" hereinafter).

7 Though three questions have been proposed in the appeal, Mr. Singh fairly submits that the appellant would press the third question, i.e., question No. (c), which reads as under :

> "(c) Whether on the facts and in the circumstances of the case and in law, the Tribunal erred in holding that there was no agency permanent establishment in the form of Taj India without appreciating that the transaction between the assessee and Taj India could not be said to be on principal to principal basis ?"

8 To appreciate the controversy in question, a brief recital of the facts is considered necessary.

9 The respondent-assessee is a registered company in Mauritius and is a tax resident of that country. The assessee is engaged in telecasting the sports channel called "Ten Sports". The assessee has appointed Taj Television (India) Private Limited, referred to hereinafter as "Taj India", as its advertising sales agent in India to sell commercial advertisement spots to prospective advertisers and other parties in India in connection with the business of programming and telecasting of Ten Sports Channel and to collect advertisement charges from the Indian advertisers. In this connection, the assessee had entered into an agreement with Taj India on May 8, 2002.

10 The assessee had also appointed Taj India as its distributor to distribute the Channel "Ten Sports" to cable systems for exhibition to subscribers in

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India. In this connection, an agreement dated March 1, 2002 was entered into between the assessee and Taj India.

11 In the assessment proceedings for the assessment year 2004-05, the Assessing Officer sought for the views of the assessee regarding non-taxability of its income in India since it did not carry any business in India through its permanent establishment (PE) and as to why it was filing an alternative computation of income. The assessee submitted reply. Referring to the India-Mauritius Double Taxation Avoidance Agreement, more particularly article 5 thereof, which defines permanent establishment, it was contended on behalf of the assessee that it was not covered by any of the clauses of the Double Taxation Avoidance Agreement and as such, it did not have a permanent establishment in India. Transactions between the assessee and Taj India are on a principal to principal basis and at arm's length prices. Taj India did not have any authority to enter into any contract on behalf of the assessee. Advertisement sales contracts were entered into between the advertisers and the assessee ; therefore, it was contended that there was no permanent establishment in India. Consequently, no further tax implication arose.

12 The Assessing Officer vide the assessment order dated December 28, 2006 however did not agree with the contention of the assessee, and after a detailed order, recorded the conclusion that Taj India had authority to conclude contracts in the name of the assessee which authority was exercised in India habitually and repeatedly. Therefore, it was held that the assessee had a permanent establishment in India within the meaning of article 5.4(i) of the Double Taxation Avoidance Agreement between India and Mauritius.

12.1. Regarding distribution of revenue, the Assessing Officer held that the same was collected through Taj India on behalf of the assessee. After considering the agreement dated March 1, 2002, the Assessing Officer held that Taj India had the exclusive right to represent the assessee before the distribution systems/cable operators and to negotiate and procure cable distribution licence agreement for the service as authorised by the assessee. Distribution of revenue collected by Taj India was shared in the ratio of 60 : 40 by the assessee and Taj India. Therefore, the Assessing Officer held that the assessee had a permanent establishment in India and the subscription revenue was taxable as business income.

13 Aggrieved by the above, the assessee preferred an appeal before the Commissioner of Income-tax (Appeals)-XXXI, Mumbai, referred to hereinafter as the "first appellate authority". In the appellate proceedings, the first appellate authority considered the two aspects, i.e., collection of advertisement revenue and revenue earned from distribution of pay channel.

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13.1. Regarding collection of advertisement revenue, the first appellate authority considered the agreement dated May 8, 2002 as well as findings returned by the Assessing Officer. Thereafter, it was held that Taj India was fully dependent on the assessee for its business. Taj India was therefore, a dependent agent. Consequently, after considering article 5(4) of the Double Taxation Avoidance Agreement, the first appellate authority vide the appellate order dated October 17, 2007 agreed with the Assessing Officer that the assessee had agency permanent establishment in India as per article 5(4) for collection of advertisement revenue. Consequently, the finding of the Assessing Officer in this regard was sustained.

13.2. Regarding distribution of revenue, the first appellate authority examined the distribution agreement entered into between the assessee and Taj India on March 1, 2002 wherefrom he deduced that Taj India was appointed as the exclusive distributor in India. Taj India was not acting as agent of the assessee but had obtained right of distribution for television channel for itself. It was found by the first appellate authority that Taj India had subsequently entered into contracts with other parties in its own name. One such contract was examined ; whereafter the first appellate authority noted that in such contract, the assessee did not figure at all. He, therefore, came to the conclusion that the assessee had given distribution rights to Taj India for promoting and distributing television channels in India on principal to principal basis. He opined that Taj India was not acting as agent of the assessee in India and the distribution agreement had given exclusive rights to Taj India to distribute the channel in India on its own behalf and not on behalf of the assessee. In such circumstances, it was held that Taj India did not constitute an agency permanent establishment within the meaning of article 5(4) of the Double Taxation Avoidance Agreement in respect of the distribution income. To this effect, the finding of the Assessing Officer was set aside.

14 Assailing the order of the first appellate authority, both the Revenue and the assessee preferred separate appeals before the Tribunal. While the Revenue's appeal being I. T. A. No. 412/Mumbai/2008 was against the finding of the first appellate authority as regards the distribution revenue, the appeal by the assessee being I. T. A. No. 5536/Mumbai/2008 was regarding collection of advertisement revenue.

15 In so far as the assessee's appeal, i.e., I. T. A. No. 5536/Mumbai/2008 is concerned, the same was dismissed as being time barred. Regarding the appeal by the Revenue on the issue of distribution revenue, i.e., I. T. A. No. 412/Mumbai/2008, the Tribunal held that none of the conditions as stipulated in article 5(4) of the Double Taxation Avoidance Agreement was

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applicable because Taj India was acting independently qua its distribution rights and the entire agreement was on principal to principal basis. Therefore, the distribution income by the assessee could not be taxed in India because Taj India did not constitute an agency permanent establishment under the terms of the said article. This finding of the first appellate authority was upheld and the challenge made thereto by the Revenue was dismissed.

15.1. Hence, the Revenue is before us in appeal. The assessee has not preferred further appeal against dismissal of its appeal.

16 Learned counsel for the parties have made detailed submissions and have taken us to the orders passed by the authorities below. They have also referred to the various provisions of the Double Taxation Avoidance Agreement, more particularly article 5 thereof.

17 Submissions made by learned counsel for the parties have been considered ; also perused the materials on record.

18 At the outset, we may advert to the Double Taxation Avoidance Agreement entered into between India and Mauritius. The said agreement was entered into between the two countries for avoidance of double taxation and for prevention of fiscal evasion with respect to taxes on income and capital gains and also to encourage mutual trade and investment. The Central Government in exercise of the powers conferred by section 90 of the Act and section 24A of the Companies (Profits) Surtax Act, 1964 issued notification dated December 6, 1983 ([1984] 146 ITR (St.) 214) (as amended) directing that all the provisions of the said Double Taxation Avoidance Agreement shall be given effect to in the Union of India.

19 As per article 3(1)(c), the expressions "a Contracting State" an "the other Contracting State" mean India or Mauritius as the context requires. Article 5 thereof defines "permanent establishment". Clause 1 says that the term "permanent establishment" means a fixed place of business through which the business of the enterprise is wholly or partly carried on. As per clause 2, which is an inclusive provision, the term "permanent establishment" shall include a place of management ; a branch ; an office ; a factory ; a workshop ; a warehouse in relation to a person providing storage facilities to others ; a mine, an oil or gas well, a quarry or any other place of extraction of natural resources ; a firm, plantation or other place where agricultural, forestry, plantation or related activities are carried out ; and a building site or construction or assembly project or supervisory activities in connection therewith, where such site, project or supervisory activity continues for a period of more than nine months. Clause 3 provides the exclusions to the term "permanent establishment".

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20 Clause 4 is relevant and is extracted hereunder :

> "4. Notwithstanding the provisions of paragraphs (1) and (2) of this article, a person acting in a Contracting State for or on behalf of an enterprise of the other Contracting State (other than an agent of an independent status to whom the provisions of paragraph 5 apply) shall be deemed to be a permanent establishment of that enterprise in the first-mentioned State if :
>
> (i) he has and habitually exercises in that first-mentioned State, an authority to conclude contracts in the name of the enterprise, unless his activities are limited to the purchase of goods or merchandise for the enterprise ; or
>
> (ii) he habitually maintains in that first-mentioned State a stock of goods or merchandise belonging to the enterprise from which he regularly fulfils orders on behalf of the enterprise."

20.1. Clause 4 starts with a non obstante clause. It starts with the word "notwithstanding" the provisions of paragraphs 1 and 2 of article 5, a person acting in a Contracting State for or on behalf of an enterprise of the other Contracting State shall be deemed to be a permanent establishment of that enterprise in the first-mentioned State if the two conditions are fulfilled. Firstly, he has and habitually exercises in the first-mentioned State, an authority to conclude contracts in the name of the enterprise, unless his activities are limited to the purchase of goods or merchandise for the enterprise. Secondly, he habitually maintains in that first mentioned State, a stock of goods or merchandise belonging to the enterprise from which he regularly fulfils orders on behalf of the enterprise. Thus, the sum and substance of clause 4 of article 5 is that a person acting in a Contracting State on behalf of an enterprise of the other Contracting State shall be deemed to be a permanent establishment of that enterprise in the first-mentioned Contracting State if he habitually exercises in the first Contracting State an authority to conclude contracts in the name of the enterprise and he habitually maintains in the first Contracting State a stock of goods or merchandise belonging to the enterprise from which he regularly fulfils orders on behalf of the enterprise.

21 Having noted the requirement of article 5 of the Double Taxation Avoidance Agreement, we may now advert as to how the matter was dealt with by the first appellate authority. As already noticed above, in so far as advertisement revenue is concerned, the first appellate authority concurred with the findings of the Assessing Officer that the assessee had an agency permanent establishment in India which is Taj India within the meaning of article 5(4) of the Double Taxation Avoidance Agreement. Therefore, this part of the income was liable to be taxed in India.

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21.1. In so far as revenue earned by Taj India on account of distribution of pay channel, the first appellate authority held as under :

"3.3 I have examined the arguments of the authorised representative and I have also examined the facts. The authorised representative filed the distribution agreement, and copies of agreement entered into by the distributor with the cable operators. The authorised representative had explained that a sub-distributor agreement was entered into between Taj India and HMA Udyog Ltd. on March 11, 2002. Copy of this agreement has been filed. Agreements with the cable operators are entered into by the sub-distributor. A sample copy of the same has also been filed. I have examined the distribution agreement between the appellant and Taj India. A perusal of the agreement reveals that the appellant has appointed Taj India as exclusive distributor in India. Further agreement provides that the appellant shall not transmit for cable distribution, any other ten sports channel service that is not distributed in cable in India by Taj India. In other words, Taj India is the exclusive distributor and prohibits the appellant from entering into distribution agreement with anybody else. Para-1.2 of the agreement provides that the Taj India shall have the exclusive right to represent Taj and negotiate and procure cable distribution and licence agreement.

Para-3.8 provides that Taj India shall be solely responsible for marketing and promoting the service to help drive the cable operators' sales. The amount and type of the said marketing support shall be at the discretion of Taj India. The responsibility of the appellant would be of providing the services signal to Taj India. Para-7 of the agreement provides that Taj India shall have the first right to negotiate and additional 3 year term for the contract.

3.4. A perusal of the distribution agreement clearly provides that Taj India is not acting as an agent of the appellant but has obtained the right of distribution of television channel for itself and subsequently it is entering into contract with other parties in its own name. This fact is proved by the cable sub-distribution agreement dated March 11, 2002 entered into between Taj India and HMA Udyog Ltd., which has appointed HMA Udyog Ltd. as sub-distributor in India. As per the agreement, 75 per cent. of the revenue would be the income of Taj India and balance 25 per cent. would be the income of HMA Udyog Ltd. In this agreement the appellant does not figure anywhere. The agreement is entered into between Taj India and HMA Udyog for distribution of television channel Ten Sports' in India. Subsequently,

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agreement is entered into between cable operators and sub-distributor. A sample copy has been filed of agreement dated October 12, 2002 between Agny Associates and Mr. Prakash S. for the distribution of television channel on the cable network. Neither the appellant nor Taj India appear anywhere in the agreement. Therefore, from the perusal of the distribution agreement, sub-distribution agreement and the cable operator agreement, it becomes very clear that the appellant has given the distribution rights to Taj India for promoting and distributing the television channel in India on principal to principal basis. Taj India subsequently has given sub-distribution rights to other parties, which have in turn entered into contract with the cable operators for the distribution of television channel. No evidence is available to show that Taj India is acting as an agent of the appellant for the distribution business. A perusal of the assessment order reveals that the Assessing Officer has provided no reason why Taj India should be treated as an agency permanent establishment for the distribution income as per article 5(4) of the Double Taxation Avoidance Agreement. I am accordingly of the opinion that Taj India is not acting as an agent of the appellant in India and the distribution agreement has given exclusive right to Taj India to distribute the channel in India on its own behalf and not on behalf of the appellant. Contracts entered into by the Taj India are by virtue of Taj India being a distributor and not an agent of appellant. In view of this it is held that Taj India does not constitute an agency permanent establishment within the meaning of article 5(4) of the Double Taxation Avoidance Agreement in respect of distribution income. In the preceding assessment year 2003-04, my predecessor Commissioner of Income-tax (Appeals) had similarly set aside the findings of the Assessing Officer on this issue in para No. 2.8 of his order dated February 26, 2007 in Appeal No. CIT(A) XXXI/ DDIT(IT)2(1)/IT-116/2006-07. I am in agreement with his findings on this issue. The findings of the Assessing Officer in this regard are set aside."

22 The first appellate authority examined the distribution agreement between the assessee and Taj India, which disclosed that Taj India was appointed as the exclusive distributor in India, Taj India being solely responsible for marketing and promoting the service to help drive cable operators' sales. Thus, the first appellate authority held that Taj India was not acting as an agent of the assessee but had obtained the right of distribution of television channel for itself. It was also noticed that Taj India had independently entered into contract with other parties for the purpose

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of distribution of pay channel and in such contracts, the assessee did not figure at all. Therefore, the first appellate authority held that the assessee had given distribution rights to Taj India for promoting and distributing television channel in India on principal to principal basis and there was no reason why Taj India should be treated as agency permanent establishment for the purpose of distribution income as per article 5(4) of the Double Taxation Avoidance Agreement. Therefore, the order of the Assessing Officer was set aside.

23 In further appeal before the Tribunal, it was held as under :

"17. We have carefully considered the entire gamut of facts as discussed in the impugned orders, rival submissions made before us, materials relied upon and the decisions relied upon. The assessee-company is incorporated and registered under the Mauritius Law and is also the tax resident of Mauritius, therefore, qua its various streams of income, India-Mauritius Double Taxation Avoidance Agreement has to be seen. The assessee is engaged in the business of telecasting sports channel called 'Ten Sports' and for generating revenue, it has been collecting advertisement revenue and distribution of channel in India. It has appointed Taj India as its advertising sales agent to sell commercial slot/spot to the prospective advertisers and other parties in India in connection with the business of programming and telecasting of 'Ten Sports' Channel. As per the agreement, commission at 10 per cent. of the advertisement revenue was paid to Taj India. The assessee has claimed that, such an income is not taxable in India, because there is no permanent establishment in India as Taj India is not a dependent agent of the assessee within the terms of article 5(4). This contention of the assessee has been negated by the learned Commissioner of Income-tax (Appeals) after discussing the issue in detail and holding that, there is no agency relationship between the assessee and the Taj India qua the advertisement income within the scope of article 5(4). However, in the Revenue's appeal, the main issue involved in ground No. 1 is with regard to taxability of distribution revenue in terms of 'distribution agreement' dated March 1, 2002. Under the terms of the distribution agreement, the assessee has appointed Taj India as exclusive distributor in India and prohibits the assessee for entering into distribution agreement with anybody else. The learned Commissioner of Income-tax (Appeals) after taking note of the 'distribution agreement' and examining various terms and clauses used therein and also taking into consideration the conduct of the parties, came to the conclusion that, Taj India is not acting as

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agent of the assessee but it had obtained the right of distribution of channel for itself and subsequently it is entering into contract with other parties in its own name in which the assessee is not a party. The distribution of the revenue between the assessee and Taj India has been allocated in the ratio of 60 : 40 and the entire relationship is principal to principal basis. The learned Commissioner of Income-tax (Appeals) has also noted that, there is no evidence on record to show that Taj India was acting as agent of the assessee for the distribution business in any manner. This finding of fact of the learned Commissioner of Income-tax (Appeals) is corroborated by the terms and conditions of the distribution agreement as well as sub-distributor agreement as placed in the paper book. Thus, such a finding of fact by the learned Commissioner of Income-tax (Appeals) without there being any rebuttal by way of any contrary material, is affirmed. Even if we independently examine the facts of the case, vis-a-vis, the provisions contained in article 5(4) to 5(6) which deals with the agency permanent establishment, it can be seen that there is no agency permanent establishment of the assessee in India. Relevant article 5 dealing with the agency permanent establishment is reproduced hereunder :

'4. Notwithstanding the provisions of paragraphs 1 and 2 of this article, a person acting in a Contracting State for or on behalf of an enterprise of the other Contracting State (other than an agent of an independent status to whom the provisions of paragraph 5 apply) shall be deemed to be a permanent establishment of that enterprise in the first-mentioned State if :

(i) he has and habitually exercises in that first-mentioned State, an authority to conclude contracts in the name of the enterprise, unless his activities are limited to the purchase of goods or merchandise for the enterprise ; or

(ii) he habitually maintains in that first-mentioned State a stock of goods or merchandise belonging to the enterprise from which he regularly fulfils orders on behalf of the enterprise.

5. An enterprise of a Contracting State shall not be deemed to have a permanent establishment in the other Contracting State merely because it carries on business in that other State through a broker, general commission agent or any other agent of an independent status, where such persons are acting in the ordinary course of their business. However, when the activities of such an agent are devoted exclusively or almost exclusively on behalf of that enterprise, he will

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not be considered an agent of an independent status within the meaning of this paragraph.

6. The fact that a company, which is a resident of a Contracting State controls or is controlled by a company which is a resident of the other Contracting State, or which carries on business in that other Contracting State (whether through a permanent establishment or otherwise) shall not, of itself, constitute either company a permanent establishment of the other.'

Thus, an agent is deemed to be a permanent establishment of a foreign enterprise, if he is not independent and habitually exercises an authority to conclude contracts in the name of the enterprise unless the activities of such person are limited to those mentioned in paragraph 4 that is, to the purchase of goods or merchandise for the enterprise ; or if he has no such authority, but habitually maintains a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the enterprise. Thus, the character of an agent, who can be said to be a dependent only if, firstly, the commercial activity for the enterprise is subject to instructions or comprehensive control and secondly, he does not bear the entrepreneur risk. It is sufficient for the establishment of an agency permanent establishment that the agent has sufficient authority to bind the enterprise's participation in the business activity. Here in this case, none of the conditions as stipulated in article 5(4) is applicable because Taj India is acting independently qua its distribution rights and the entire agreement ostensibly is on principal to principal basis as analyzed and found by the learned Commissioner of Income-tax (Appeals). When the entire relationship qua the distribution revenue is that of principal to principal basis and the Taj India is acting independently, then it moves out from the conditions laid down in article 5(4). Thus the distribution income by the assessee cannot be taxed in India, because Taj India does not constitute an agency permanent establishment under the terms of article 5(4). Thus, the order of the Commissioner of Income-tax (Appeals) is upheld and ground No. 1 as raised by the Revenue is dismissed."

24 The Tribunal noted that the first appellate authority, after due deliberation, had returned a finding of fact that Taj India was not acting as agent of the assessee but it had obtained the right of distribution of the channel for itself and subsequently, it had entered into contracts with other parties in its own name in which the assessee was not a party. The distribution of the revenue between the assessee and Taj India was in the ratio of 60 : 40

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and the entire relationship was on principal to principal basis. The Tribunal noted that this finding by the first appellate authority is corroborated by the terms and conditions of the distribution agreement as well as the sub-distributor agreement. After examining the requirement of article 5 of the Double Taxation Avoidance Agreement to constitute agency permanent establishment, the Tribunal as a matter of fact held that none of the conditions as stipulated in article 5(4) was applicable because Taj India was acting independently qua its distribution rights and the entire agreement was on principal to principal basis. Therefore, it was held that the distribution income earned by the assessee cannot be taxed in India because Taj India does not constitute an agency permanent establishment under the terms of article 5(4) of the Double Taxation Avoidance Agreement. The order of the first appellate authority was accordingly upheld.

25 On thorough consideration of the matter, we are in agreement with the views expressed by the Tribunal. In fact, there is concurrent finding of fact between both the appellate authorities on this point. Learned standing counsel, Revenue has not been able to show any perversity in such finding returned by the appellate authorities. In the absence thereof, we see no good reason to interfere with the finding of the Tribunal affirming the order of the first appellate authority.

26 Consequently, we do not find any merit in the appeal. No substantial question of law arises from the order of the Tribunal. The appeal is accordingly dismissed. However, there shall be no order as to costs.

27 In view of the above, the other appeal being Income Tax Appeal No. 1437 of 2017 is also dismissed.

[2020] 425 ITR 153 (Bom)

[IN THE BOMBAY HIGH COURT — PANAJI BENCH]

AFONSO REAL ESTATE DEVELOPERS

v.

COMMISSIONER OF INCOME-TAX AND ANOTHER

M. S. SONAK and **NUTAN D. SARDESSAI** JJ.

February 21, 2020.

SS ▸ ITA, 1961 ss 28, 45
AY ▸ 2007-08
HF ▸ Department

BUSINESS—CAPITAL GAINS—BUSINESS INCOME OR CAPITAL GAINS—FINDING THAT OBJECT OF ASSESSEE-FIRM WAS TO PURCHASE AND SELL

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LAND—PROFIT FROM PURCHASE AND SALE OF LAND ASSESSABLE AS BUSINESS INCOME—INCOME-TAX ACT, 1961, SS. 28, 45.

Held, *that the business of the assessee very specifically included buying and selling properties situated in various places in Goa either wholly or in plots. Considering the wide phraseology employed, it was obvious that the business of the assessee included buying and selling even agricultural properties. Besides, both the Assessing Officer and the Commissioner (Appeals) had noted that by the sale deed, the assessee sold not merely the agricultural property but also another property admeasuring 2,525 sq.mtrs. to H. Therefore, this was not a case of sale of a solitary property, by way of a one off transaction. The gains from sale of land were assessable as business income. The finding of fact could not be regarded as perverse, so as to give rise to any substantial question of law.*

NARAIN SWADESHI WEAVING MILLS *v.* CEPT [1954] 26 ITR 765 (SC) *distinguished.*

NARAIN SWADESHI WEAVING MILLS *v.* CEPT [1954] 26 ITR 765 (SC) (para 11) *referred to.*

Tax Appeal No. 30 of 2013.

S. R. Rivonkar, Senior Advocate, *Ms. N. Rivonkar*, Advocate, for the appellant.

Ms. Amira Razaq, Standing Counsel, for the respondents.

JUDGMENT[1]

The judgment of the court was delivered by

1 M. S. SONAK J.—Heard Mr. S. R. Rivonkar, learned senior advocate along with Ms. N. Rivonkar for the appellant and Ms. Amira Razaq, learned standing counsel for the Income-tax Department-respondent.

2 On December 10, 2013, this appeal was admitted on the following substantial questions of law :

> "(i) Whether the learned Tribunal was right in holding that transaction is a business transaction when there was only one transaction and not series of transactions ?
>
> (ii) Whether the learned Tribunal has correctly interpreted the provisions of section 2(14) of the Income-tax Act ?"

3 Mr. S. R. Rivonkar, learned senior advocate for the appellant submits that in fact, only the substantial question of law at (i) above arises for determination and should the same be answered in favour of the appellant,

1. Oral judgment.

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then, the impugned judgment and order dated August 23, 2013 made by the Income-tax Appellate Tribunal (ITAT) will have to be set aside and the order of the Commissioner of Income-tax (Appeals) dated March 26, 2013 will have to be restored.

4 Ms. Amira Razaq, learned standing counsel for the respondent also accepts that the aforesaid position stated by Mr. Rivonkar is correct. Hence, we proceed to decide only the first substantial question of law which arises in the present appeal.

5 The appellant-assessee is a partnership firm constituted vide partnership deed dated July 29, 1989. This firm was however registered only on April 4, 2006, about which there is no serious dispute. The record indicates that the firm had acquired agricultural land at Cavelossim admeasuring 28,200 sq.mtrs. vide a deed of exchange dated August 15, 1990. This land along with another property admeasuring 2,525 sq.mtrs., was sold by the appellant-assessee vide sale deed dated July 13, 2006 to Headway Resorts Line Pvt. Ltd. Company for a total consideration of Rs. 1,69,20,000.

6 The appellant-assessee filed return of income on January 30, 2008 for the assessment year 2007-08 declaring a total income of Rs. 1,57,069, claiming deduction to the extent of Rs. 1,69,20,000, inter alia, on the ground that the amount received towards the sale of the properties were assessable as long-term capital gains which were entitled to be deducted in terms of sections 54E and 54EC of the Income-tax Act, 1961 (I.T. Act).

7 The Assessing Officer (AO) did not agree with the contention of the appellant-assessee, inter alia, on the ground that the Cavelossim property fell within a distance of 8 kms. from the limits of the Margao Municipal Council. The appellant-assessee appealed to the Commissioner of Income-tax (Appeals) vide I. T. A. No. 163/MRG/10 (the assessment year 2007-08).

8 Soon thereafter, respondent No. 2 issued notices under sections 147 and 148 of the Income-tax Act to the appellant-assessee seeking to reopen the assessment for the assessment year 2007-08. After hearing the assessee, a revised assessment order was made on February 21, 2011 computing the entire income of the appellant-assessee as "business income" and bringing the same to tax. The appellant-assessee therefore, preferred yet another appeal being I. T. A. No. 348/MRG/10-11 to the Commissioner of Income-tax (Appeals).

9 The Commissioner of Income-tax (Appeals), disposed of both the appeals by a common judgment and order dated March 26, 2013. Both the appeals were allowed and the orders of the Assessing Officer were set aside.

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10 The Revenue instituted appeal being I. T. A. No. 98/PNJ/2013 before the Income-tax Appellate Tribunal to question the common judgment and order dated March 26, 2013 made by the Commissioner of Income-tax (Appeals). The appellant-assessee filed cross-objections which were numbered as 26/PNJ/2013. The Income-tax Appellate Tribunal vide common order dated August 23, 2013 allowed the Revenue's appeal and dismissed the cross-objections of the appellant-assessee, thereby, restoring the orders made by the Assessing Officer that the income derived by the appellant-assessee from the sale of the properties was "business income". Hence the present appeal on the aforesaid substantial question of law.

11 Mr. Rivonkar, the learned senior advocate for the appellant submits that the business of the appellant-assessee was to develop properties into plots or by constructing buildings and thereafter engage in the real estate business. He submits that the fact that the agricultural land was purchased in the year 1990 and the same was not even converted suggests that the appellant-assessee was not carrying on any business in relation to such property. He submits that on the basis of a single transaction of this nature, it could not have been held that the appellant-assessee was carrying on business in selling and purchasing properties. He submits that there is absolutely no material on record to establish that the appellant-assessee was engaged in the business of selling and purchasing agricultural properties and therefore, the Income-tax Appellate Tribunal, was not at all right in recording a finding that the proceeds from sale constitute income from business. He relied upon the decision of the Supreme Court in *Narain Swadeshi Weaving Mills* v. *CEPT* [1954] 26 ITR 765 (SC) ; AIR 1955 SC 176.

12 On the other hand, Ms. Razaq defends the impugned judgment and order made by the Income-tax Appellate Tribunal on the basis of the reasoning reflected therein. She submits that the finding recorded by the Income-tax Appellate Tribunal is borne out by the material on record and therefore warrants no interference in this appeal.

13 The rival contentions now fall for our determination.

14 The main issue involved in this appeal is whether the proceeds from sale of the properties vide sale deed dated July 13, 2006 can be regarded as income from business or not.

15 The appellant-assessee was constituted vide deed of partnership dated July 29, 1989. The business of the partnership is that of real estate developers. Clause 2 of the partnership deed is most relevant and the same reads as follows :

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> "2. The business of the partnership firm shall be that of buying and developing the properties into plots including construction works and/or any other business as the parties hereto may mutually agree upon from time to time. The business shall include buying or selling of properties situated at various places in Goa either wholly or in plots."

16 From the aforesaid, it is quite clear that the business of the appellant-assessee is buying and selling properties situated in various places in Goa either wholly or in plots. Mr. Rivonkar's contention that the business of the appellant-assessee is only to purchase properties, develop them into plots or construct buildings upon them and thereafter to sell them cannot be accepted, looking to the aforesaid provisions in the deed of partnership by which the appellant-assessee came to be constituted. The business of the appellant-assessee very specifically includes buying and selling properties situated in various places in Goa either wholly or in plots. Considering the wide phraseology employed, it is obvious that the business of the appellant-assessee includes buying and selling of even agricultural properties. Accordingly, we are unable to accept that the sale of the properties by the appellant-assessee vide sale deed dated July 13, 2006 has no nexus with the business of the appellant-assessee.

17 Besides, we find that both the Assessing Officer as well as the Commissioner of Income-tax (Appeals) have noted that by sale deed dated July 13, 2006, the appellant-assessee sold not merely the agricultural property but also another property admeasuring 2,525 sq. mtrs. to Headway Resort Line Pvt. Ltd. Therefore, this is not a case of sale of a solitary property, by way of a one off transaction. The appellant-assessee, in terms of clause 2 of the partnership deed is clearly involved in buying and selling properties situated in various places in Goa either wholly or in plots. By sale deed dated July 13, 2006, the appellant-assessee has indeed sold the properties purchased by it for a considerable profit. This material, according to us, is more than sufficient to sustain the findings recorded by the Assessing Officer and the Income-tax Appellate Tribunal. The finding of fact cannot be regarded as perverse, so as to give rise to any substantial question of law or so as to warrant interference.

18 The decision in *Narain Swadeshi Wvg. Mills* case (supra), is entirely distinguishable, since, it turns on its own peculiar facts. There, the assessee-firm had virtually stopped its business mainly because no raw material was available due to the war. The factory premises were then leased and the issue was whether the lease rent could be treated as business profits liable to excess profits tax. In this fact situation, the hon'ble apex court held that

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such lease could not be described as the business of the assessee-firm and lease rent would therefore not qualify as business income. These facts, offer no parallel whatsoever to the fact situation in the present case.

19 We therefore answer the substantial question of law against the appellant-assessee and in favour of the respondent-Revenue.

20 The appeal is accordingly liable to be dismissed and is hereby dismissed. There shall be no order as to costs.

[2020] 425 ITR 158 (Chhattisgarh)

[IN THE CHHATTISGARH HIGH COURT]

SYSTEM INDIA CASTINGS AND OTHERS

v.

PRINCIPAL COMMISSIONER OF INCOME-TAX AND ANOTHER

PRASHANT KUMAR MISHRA J.

June 26, 2019.

SS ▸ ITA, 1961, ss 276C, 277
AY ▸ 1990-91
HF ▸ Assessee

OFFENCES AND PROSECUTION—CONCEALMENT OF INCOME—PENALTY WITH REGARD TO SAME ALLEGATIONS DELETED—PROSECUTION UNDER SECTIONS 276C AND 277 NOT VALID—INCOME-TAX ACT, 1961, SS. 276C, 277.

Since the act of concealment of income is the main constituent for the charge under sections 276C and 277 of the Income-tax Act, 1961, once the Commissioner (Appeals) concluded that there was no concealment of income on the part of the assessee, the very foundation of the charge would not survive.

K. C. BUILDERS *v.* ASST. CIT [2004] 265 ITR 562 (SC) *followed.*

K. C. BUILDERS *v.* ASST. CIT [2004] 265 ITR 562 (SC) (para 3) *referred to.*

Cr. M. P. No. 2075 of 2018.

S. Rajeshwara Rao with *M. K. Sinha*, Advocates, for the petitioners.

Ms. Naushina Ali for *A. Choudhary*, Standing Counsel, for the respondents.

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ORDER

PRASHANT KUMAR MISHRA J.—The petition is posted for hearing on admission, however, since learned standing counsel for the Income-tax Department has entered appearance on advance notice, therefore, this court proceeded to hear the matter finally with the consent of learned counsel for the parties. 1

Prayer in this petition is for quashment of proceeding of Criminal Case No. 29362 of 1996 (*ITO* v. *System India Castings*) pending before CJM, Durg. 2

At the outset, the learned standing counsel for the Department would submit that the petitioners having already moved before the trial Magistrate for dropping the proceeding, the instant petition is not maintainable. However, considering that law in respect of continuation of prosecution for commission of offence under sections 276C and 277 read with section 278 of the Income-tax Act, 1961 (for short "the Act") on a previous complaint though subsequently the fact of concealment of income having already been extinguished pursuant to the appellate order passed by the Income-tax Appellate Tribunal (for short "the Tribunal") is no longer res integra in view of the judgment rendered by the Supreme Court in the matter of *K. C. Builders* v. *Asst. CIT* [2004] 265 ITR 562 (SC) ; [2004] 2 SCC 731, therefore, this court proceeded to hear the matter on merits. 3

The subject complaint was filed by the Revenue before the CJM, Durg sometime in the year 1995 pursuant to sanction accorded by the Commissioner of Income-tax, Jabalpur under section 279 of the Act on March 30, 1995. The gravamen of the offence for which sanction was accorded is stated as under in the sanction order : 4

> "The assessee-firm is engaged in the business of manufacture of cast iron products from the cast iron scrap. For the assessment year 1990-91, the assessee furnished the return showing total income of Rs. 49,484 and the assessment was made under section 143(3) of the Income-tax Act, 1961, on March 31, 1992 at Rs. 9,23,760. The assessee claimed purchases of cast iron scraps from one M/s. Sagar Enterprises, 53, Malviya Chowk, Jabalpur, on different dates. The payment were shown to have been made in cash at Rs. 10,000 per day for 74 continuous days. After making necessary enquiries, it was found that no such concern ever existed at the abovementioned address. Further, the sales tax number on the bills was also found to be bogus after making enquiries from the Sales-tax Department. The assessee was not able to furnish receipts in respect of the payments claimed to have been made in cash. Further, no payment slips were available in

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respect of the above purchases. In one of the bills, the vehicle used for transportation was found to be a tractor trolley instead of the truck as claimed by the assessee. Further, the same tractor trolley was shown to be carrying some other goods on January 29, 1990 from Bhilai to Tedesara. It is not possible for the tractor trolley to transport cast iron scraps from Jabalpur to Tedesara on January 31, 1990 as claimed by the assessee. Based on all these discrepancies, the Assessing Officer arrived at a conclusion that there was no party named M/s. Sagar Enterprises at Jabalpur dealing in scrap and the purchases shown to have been made from the above said party was only a colourful device to introduce scrap acquired by the assessee from undisclosed sources. He accordingly, added back the investment in the purchase of the scrap at Rs. 7,51,739 to the income of the assessee. The claim of transportation expenses related to the transaction with M/s. Sagar Enterprises amounted to Rs. 42,650 was also disallowed. Additions made by the Assessing Officer have been sustained by the hon'ble Income-tax Appellate Tribunal, Nagpur Bench, Nagpur, vide its order dated March 19, 1993 in I. T. A. No. 534/Nag/92.

Consequently, penalty of Rs. 4,26,630 under section 271(1)(c) of the Income-tax Act, 1961 has also been levied by the Assessing Officer vide order dated September 20, 1993. The assessee has preferred an appeal against the penalty order before the Commissioner of Income-tax (Appeals), Raipur which is pending for decision.

Now therefore, in exercise of the powers conferred on me by virtue of section 279 of the Income-tax Act, 1961 I, B. P. Misra, Commissioner of Income-tax, Jabalpur (M.P.), hereby accord sanction to prosecute and to proceed against the abovementioned persons by filing a complaint for the offence stated hereinabove in the court of competent jurisdiction."

5 It is thus manifest that in the sanction order itself, it was mentioned that the assessee has preferred an appeal against the penalty order before the Commissioner of Income-tax (Appeals), Raipur, which is pending for decision. When the Commissioner of Income-tax (Appeals) heard the appeal preferred by the assessee on merits, it reached the conclusion that the petitioner has not concealed his income, therefore, penalty of Rs. 4,26,630 deserves to be cancelled. Since the act of concealment of income is the main constituent for charge under sections 276C and 277 of the Act, once the Commissioner of Income-tax (Appeals) concluded that there was no concealment of income on the part of the assessee, the very foundation of the charge would not survive. It is also to be noted that against the order

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passed by the Commissioner of Income-tax (Appeals) deleting the penalty, the Revenue preferred second appeal before the Tribunal, Nagpur. However, the appeal filed by the Revenue was dismissed by order dated June 12, 1997 (annexure-P-10). The Revenue did not take up the matter further and thus the order passed by the Tribunal affirming the order passed by the Commissioner of Income-tax (Appeals) has attained finality.

6 In the matter of *K. C. Builders* v. *Asst. CIT* (supra), the Supreme Court was faced with similar situation. Considering the petition filed by the assessee, the Supreme Court held in para 26 that once the finding of concealment and subsequent levy of penalties under section 271(1)(c) of the Act has been struck down by the Tribunal, the Assessing Officer has no other alternative except to correct his order under section 154 of the Act as per the directions of the Tribunal. The subject matter of the complaint before the Supreme Court being concealment of income arrived at on the basis of the finding of the Assessing Officer, if the Tribunal has set aside the order of concealment and penalties, there is no concealment in the eye of law and, therefore, the prosecution cannot be proceeded with by the complainant and further proceedings will be illegal and without jurisdiction. The Supreme Court further observed that if the trial is allowed to proceed further after the order of the Tribunal and the consequent cancellation of penalty, it will be an idle and empty formality to require the appellants to have the order of the Tribunal exhibited as a defence document inasmuch as the passing of the order as aforementioned is unsustainable and unquestionable.

7 Before the above observations in para 26, the Supreme Court would observe in para 23 that the High Court is not justified in dismissing the criminal revision petition ignoring the settled law as laid down by the Supreme Court that the finding of the Appellate Tribunal was conclusive and the prosecution cannot be sustained since the penalty after having been deleted by the complainant following the Appellate Tribunal's order, no offence survives under the Income-tax Act and thus "quashing of prosecution is automatic". The same expression has again been used by the Supreme Court in para 24 also.

8 In view of the settled legal position as enunciated by the Supreme Court in the matter of *K. C. Builders* v. *Asst. CIT* (supra), it will be an empty formality to direct the petitioners to approach the trial Magistrate, who has otherwise kept the application preferred by the petitioners pending since January 15, 2014.

9 In the circumstances, this court deems it appropriate to exercise its inherent power for quashing the proceeding of Criminal Case No. 29362 of

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1996 (*ITO* v. *System India Castings*) pending before CJM, Durg and it is accordingly quashed.

10 The instant petition is accordingly allowed.

[2020] 425 ITR 162 (Guj)

[IN THE GUJARAT HIGH COURT]

NIRANJAN CHIMANLAL JANI

v.

DEPUTY COMMISSIONER OF INCOME-TAX

AKIL KURESHI and **B. N. KARIA** JJ.

February 21, 2018.

SS ▶ ITA 1961, ss 45, 147, 148
AY ▶ 2012-13
HF ▶ Assessee

REASSESSMENT—NOTICE—VALIDITY—REOPENING ON GROUND INCOME ESCAPED ASSESSMENT ON ACCOUNT OF LONG-TERM CAPITAL GAINS—IMPROVEMENT COST ON LAND DULY SUBSTANTIATED AND EXAMINED BY ASSESSING OFFICER IN ORIGINAL ASSESSMENT—REOPENING CANNOT BE PERMITTED—NOTICE QUASHED—INCOME-TAX ACT, 1961, SS. 45, 147, 148.

For the assessment year 2012-13, the assessee declared, inter alia, income on account of long-term capital gains that arose out of sale of agricultural land. The Assessing Officer examined the transaction of the sale of immovable property and other sundry incomes and passed an order under section 143(3) of the Income-tax Act, 1961 making no change in the assessee's declaration of capital gains. The Assessing Officer issued a notice under section 148 on the ground that the assessee had earned long-term capital gains after claiming deduction of cost of improvement on the land sold, that though the cost of the land was mentioned, there was nothing in the balance-sheet to indicate that the assessee had incurred any expenditure on the land sold and therefore, income had escaped assessment in the assessment year 2012-13. The objections raised by the assessee were rejected by the Assessing Officer. On a writ petition :

Held, *allowing the petition, that it was only after examination of the sale transaction of the land and related issues, that the Assessing Officer had passed the order under section 143(3) making no disallowance on account of the long-term capital gains. The entire issue had been minutely examined by the Assessing Officer and therefore, he could not be allowed to reopen the*

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assessment. The assessee had submitted to the Assessing Officer that he had purchased the agricultural land for a cost of Rs. 81,000 and had sold it for Rs. 2.15 crores during the assessment year 2012-13 and the assessee's books of account as well as his return duly reflected the sum of Rs. 5.09 lakhs expended in the year 1987-88, on the basis of which, the assessee claimed indexed cost by way of deduction. Along with the sale deed, the assessee had also filed a report of the valuer who had estimated the cost of construction of staff room, office, godown, labourers' rooms, compound wall, borewell, etc., at Rs. 5.09 lakhs. The reasons recorded lacked validity and there was lack of application of mind on the part of the Assessing Officer when he had conveyed that the cost of improvement of Rs. 5.09 lakhs was not reflected in the assessee's books of account. The notice issued under section 148 for reopening the assessment was quashed.

Special Civil Application No. 18742 of 2017.

Darshan R. Patel, Advocate, for the petitioner.

Mrs. Mauna M. Bhatt, Advocate, for the respondent.

JUDGMENT[1]

The judgment of the court was delivered by

AKIL KURESHI J.—The petitioner has challenged a notice dated March 3, 2017 issued by the respondent-Assessing Officer to reopen the petitioner's assessment for the assessment year 2012-13. **1**

The brief facts are as under : **2**

The petitioner is an individual. For the assessment year 2012-13, the petitioner had filed the return of income disclosing total income of Rs. 1.22 crores (rounded off). This comprised of a long-term capital gains arising out of sale of immovable property besides other sundry incomes. The return was taken in scrutiny by the Assessing Officer, during which, the Assessing Officer examined the transaction of sale of agricultural land of the petitioner situated at Hathijan which led to the assessee earning capital gains. The Assessing Officer passed an order of assessment under section 143(3) of the Act on January 19, 2015. In such order, the Assessing Officer made no change in the petitioner's declaration of capital gains. **3**

To reopen such assessment, the Assessing Officer issued impugned notice. In order to do so, he had recorded the following reasons : **4**

> "In this case, the assessee had filed his return of income for the assessment year 2012-13 on September 26, 2012 declaring total income of Rs. 1,22,00,280. The assessment have been completed and

1. Oral judgment.

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income was determined at Rs. 1,22,08,700 vide order dated January 19, 2015.

Scrutiny of computation of income and submission dated December 15, 2014 revealed that the assessee has earned long-term capital gains amounting to Rs. 1,84,12,333 after claiming deduction of Rs. 26,63,737 as cost of improvement on Hathijan Land. For claiming improvement cost, the assessee has furnished copy of personal balance-sheet of the financial year 2010-11 depicting cost of improvement of Rs. 5,09,000 on this Hathijan land. It was noticed from the audited balance-sheet furnished by the assessee for the financial year 2010-11 that though the cost of Hathijan land was mentioned, there was nothing in the balance-sheet to indicate that the assessee has incurred any expenditure on this land.

In view of the above, I am satisfied that there is under-assessment in this case for the relevant assessment year 2012-13. I therefore have reasons to believe that Rs. 26,63,737 has escaped assessment within the meaning of section 147 of the Income-tax Act, 1961 and is a fit case for reopening under section 147 of the Income-tax Act, 1961. The case is reopened after approval from the Joint CIT, Range-1(2), Ahmedabad, vide his letter bearing No. Joint CIT/R1(2)/Ahm/Revenue Audit Objection/148/2016-17 dated March 1, 2017."

5 The petitioner raised objections to the notice of reopening under a communication dated September 13, 2017. Such objections were rejected by the Assessing Officer on September 18, 2017. Hence, this petition.

6 Appearing for the petitioner, the counsel Shri Darshan Patel raised the following contentions :

I. The entire issue was scrutinised by the Assessing Officer during the original assessment proceedings. Any attempt on his part to make any changes in the order of assessment would amount to a change of opinion.

II. The issue was raised by the Assessing Officer at the instance of the audit party, without there being any conviction on his part that income chargeable to tax has escaped assessment.

III. Even otherwise, the reasons recorded by the Assessing Officer are incorrect. The petitioner had showed the cost of improvement of Rs. 5.09 lakhs expanded in the year 1987-88 and had claimed indexation thereof due to passage of time.

7 On the other hand, learned counsel Mrs. Mauna Bhatt for the Department opposed the petition contending that the Assessing Officer had recorded proper reasons before issuing the notice. The cost of improve-

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ment of Rs. 5.09 lakhs was not reflected in the accounts of the assessee. The notice has been issued within a period of four years.

8 Having heard learned advocates for the parties and having perused the documents on record, we notice that during the original assessment, the Assessing Officer had raised multiple queries. One of them, as is apparent from the petitioner's response to the Assessing Officer dated December 15, 2014, pertained to the sale of the property in question. We may recall, the petitioner had sold agricultural land situated at village Hathijan during the said year. In his written communication dated December 15, 2014, the petitioner pointed out to the Assessing Officer that he had purchased the said land for cost of Rs. 81,000 under a registered sale deed and sold the same for Rs. 2.15 crores during the current year. Since the purchaser is not an agriculturist, he had made an agreement and the sale deed would be executed after conversion of the land into non-agricultural use. With respect to cost of improvement, he stated as under :

> "3. *Evidence of cost of improvement*
>
> Please note that I had purchased the above land by registered agreement of sale (purchase) Banakhat for Rs. 80,816 plus expenses and total payment made by me through cross account payee cheque of Rs. 81,000 but due to one reason or the other the selling farmers had not executed final sale deed therefore the seller farmers, namely, Dhanabhai Prajapati and Bhalabhai Prajapati had prepared a registered will and the same was inherited through registered will in fact I had purchased the above agricultural property for Rs. 81,000 and possession was also taken at that time after Banakhat and after taking possession I had incurred expenses for improvement of the above land and total expenses incurred by me were Rs. 5,09,000 in the financial year 1987-88 for improvement of the above land at that time from my books so, I hereby enclosed my personal balance-sheet for the same wherein the above improvement cost of the above land are reflected in May balance-sheet."

9 It was only after such examination of the sale of the land and related issues, the Assessing Officer passed the order of assessment making no disallowance. The entire issue was thus minutely examined by him. On this count, the Assessing Officer cannot be allowed to reopen the assessment.

10 Even otherwise, we find that the reasons lack validity and there was a degree of lack of application of mind on the part of the Assessing Officer when he conveyed that the cost of improvement of Rs. 5.09 lakhs was not reflected in the assessee's books of account. The assessee's books as well as the return filed, duly reflected the sum of Rs. 5.09 lakhs expended way back

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in the year 1987-88, on the basis of which, the assessee claimed indexed cost of Rs. 26.63 lakhs by way of deduction. It appears that along with the sale deed, the petitioner had also filed a report of the valuer dated March 10, 2012 who had estimated the cost of construction of staff room, office, godown, labourers' rooms, compound wall, borewell, etc. to Rs. 5.09 lakhs.

11 In the result, the petition is allowed. The impugned notice is set aside. The petition is disposed of.

[2020] 425 ITR 166 (Bom)

[IN THE BOMBAY HIGH COURT]

COMMISSIONER OF INCOME-TAX (EXEMPTIONS)

v.

MUMBAI METROPOLITAN REGION DEVELOPMENT AUTHORITY

UJJAL BHUYAN and MILIND N. JADHAV JJ.

January 24, 2020.

SS ▸ ITA 1961, ss 2, 12AA
AY ▸ 2009-10
HF ▸ Assessee

CHARITABLE PURPOSE—REGISTRATION OF TRUSTS—CANCELLATION OF REGISTRATION—CONDITIONS PRECEDENT—VIEW THAT TRUST WOULD BE HIT BY PROVISO TO SECTION 2(15)—NOT A GROUND FOR CANCELLATION OF REGISTRATION—INCOME-TAX ACT, 1961, SS. 2, 12AA.

Section 12AA of the Income-tax Act, 1961 lays down the procedure for registration of a trust. Sub-section (3) inserted with effect from October 1, 2004, provides for cancellation of registration. Two conditions are required to be satisfied before invocation of section 12AA(3) of the Act. Firstly, the activities of the trust or institution are not genuine and secondly, the activities are not being carried out in accordance with the objects of the trust or institution. The use of the word "or" between the two conditions is indicative of the disjunctive nature of the two conditions. In other words, it is enough if one of the two conditions is satisfied. The requirement therefore is that the authority competent under section 12AA(3) to cancel registration must arrive at the satisfaction that one of the two conditions mentioned therein is attracted. Such satisfaction must be recorded as a matter of fact on the basis of specific materials on record. Merely saying that the activities of the assessee

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are hit by the proviso to section 2(15), would not lead to automatic cancellation of registration as that is not a ground provided under section 12AA(3) for cancellation of registration.

Held, *that the Tribunal recorded the finding that the order of the Director of Income-tax (Exemptions) did not disclose which activity of the assessee was not genuine or that the assessee was not genuine. The Tribunal also recorded that there was no material in the order explaining that the activities of the assessee were not being carried out in accordance with its objects. The view that the assessee was directly hit by the proviso to section 2(15) of the Act may lead to denial of exemption to the assessee in the assessment proceeding for the relevant assessment year but could not be a ground for cancellation of registration under section 12AA(3). The competent authority under section 12AA(3) must be satisfied that the activities of the trust are not genuine or that the activities are not being carried out in accordance with the objects of the trust or the institution. Such satisfaction must be recorded as a matter of fact on the basis of specific materials on record. The cancellation of registration was not valid.*

Cases referred to :

CIT *v.* Builders Association of India (I. T. A. No. 92 of 2016, dated 4-5-2018) (para 17)

CIT (Pr.) *v.* JIS Foundation [2018] 89 taxmann.com 226 (Cal) (para 18)

CIT (Pr.) *v.* JIS Foundation [2018] 96 taxmann.com 611 (SC) (para 14)

CIT *v.* Mumbai Metropolitan Regional Iron and Steel Market Committee [2018] 404 ITR 171 (Bom) (para 17)

CIT (Exemptions) *v.* Sadguru Narendra Maharaj Sansthan [2018] 407 ITR 12 (Bom) (para 17)

DIT (Exemptions) *v.* Khar Gymkhana [2016] 385 ITR 162 (Bom) (para 17)

DIT (Exemption) *v.* North Indian Association [2017] 393 ITR 206 (Bom) (para 16)

Tamilnadu Cricket Association *v.* DIT (Exemptions) [2014] 360 ITR 633 (Mad) (paras 12, 32)

Income Tax Appeal (IT) No. 2010 of 2017.

Ashok Kotangle, Standing Counsel, *Prabhakar Ranshur*, Advocate, for the appellant.

S. E. Dastur, Senior Advocate, *Madhur Agarwal* and *A. K. Jasani* for the respondent.

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JUDGMENT

1 Heard Mr. Ashok Kotangle, learned standing counsel, the Revenue for the appellant ; and Mr. S.E. Dastur, learned senior counsel along with Mr. Madhur Agarwal and Mr. A.K. Jasani, learned counsel for the respondent-assessee.

2 This appeal has been preferred by the Revenue under section 260A of the Income-tax Act, 1961 (briefly "the Act" hereinafter) against the order dated April 5, 2017 passed by the Income-tax Appellate Tribunal, "B" Bench, Mumbai (briefly "the Tribunal" hereinafter) in Income Tax Appeal No. 625/Mum/2012 for the assessment year 2009-10.

3 The appeal has been preferred on the following two questions stated to be substantial questions of law :

> "(I) Whether, on the facts and in the circumstances of the case and in law, the Tribunal was right in quashing the order passed by the Director of Income-tax (Exemptions) cancelling the registration under section 12AA(3) of the Income-tax Act, 1961 despite the fact that the activities undertaken by the assessee cannot be said to be charitable in nature in view of the proviso to section 2(15) of the said Act inserted with effect from April 1, 2009 ?
>
> (II) Whether on the facts and in the circumstances of the case and in law, the Tribunal was right in its findings at para 9 of its order in I. T. A. No. 625/Mum/2012 dated April 5, 2017, i.e., 'Since, the registration is already allowed consequently no disallowance can be made in respect to interest income and leasing activity income, i.e., the rent and other fees, because these fall under the objects of the assessee's institution and hence on merits also the assessee has a case' which is not in accordance with the provisions of section 13(8) of the Income-tax Act, 1961 ?"

4 From the above, what is discernible is that the issue involved in this appeal is cancellation of registration of the respondent by the Director of Income-tax (Exemptions) under section 12AA(3) of the Act, which order has been set aside by the Tribunal.

5 Though the facts are not in dispute, however, for proper appreciation of the controversy in question it would be apposite to briefly narrate the facts of the case.

6 The respondent is an assessee under the Act. The respondent was granted registration as a trust under section 12AA(1) of the Act.

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A proposal was received by the Director of Income-tax (Exemptions) that registration granted to the respondent under section 12AA(1) of the Act should be cancelled. **7**

Be it stated that, the respondent-assessee is the Mumbai Metropolitan Region Development Authority. As per the proposal for cancellation of registration, it was mentioned that the respondent was carrying on activities in the nature of trade, commerce or business etc. and gross receipts therefrom were in excess of Rs. 10 lakhs. Therefore, the proviso to section 2(15) of the Act was attracted from the assessment year 2009-10. **8**

A show-cause notice was issued by the office of the Director to the respondent on December 13, 2011 to show cause as to why registration granted to it should not be withdrawn by invoking the provisions of section 12AA(3) of the Act. **9**

The respondent filed written submission and was also represented by the authorised representative. **10**

By order dated December 27, 2011, the Director of Income-tax (Exemptions) took the view that the respondent was directly hit by the proviso to section 2(15) of the Act and in view of the deeming provision that when activities of the respondent were not for charitable purpose, then the trust (respondent) itself became non-genuine for the purpose of section 11 of the Act as it had lost its public charitable status and thus the provisions of section 12AA(3) got attracted. Accordingly, the Director held that the respondent had become non-genuine for the purpose of section 11 of the Act and, therefore, registration allowed to it in earlier years under section 12AA of the Act was cancelled/withdrawn with effect from the assessment year 2009-10. Accordingly the respondent was held to be a non-charitable trust/institution. **11**

Aggrieved by the cancellation of registration, the respondent preferred appeal before the Tribunal. The Tribunal after hearing the matter and following the decision of the Madras High Court in *Tamilnadu Cricket Association* v. *DIT (Exemptions)* [2014] 360 ITR 633 (Mad) set aside the order passed by the Director of Income-tax (Exemptions) vide the order dated April 5, 2017. The Tribunal held that it did not find anything in the order of the Director which held that the respondent was undertaking any activity which was not genuine or that the trust or institution was not genuine. It was further held that there were no materials on record to show that the respondent-trust or its affairs were not being carried out in accordance with the objects of the respondent-trust. Accordingly, while setting aside the order of the Director, registration of the respondent was restored. **12**

Aggrieved, the present appeal has been preferred. **13**

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14 Learned counsel for the appellant has referred to the order passed by the Director and submits that the said order clearly indicated as to why registration of the respondent was required to be cancelled. He submits that in so far as the activity of the respondent is concerned, clearly the proviso to section 2(15) of the Act was attracted, thereby rendering the respondent non-charitable. He submits that on similar issue, the Supreme Court has granted leave to file appeal in *Pr. CIT* v. *JIS Foundation* [2018] 96 taxmann.com 611 (SC). The Tribunal was not justified in interfering with the reasoned order passed by the Director.

15 On the other hand, Mr. Dastur, learned senior counsel submits that since the impugned order was passed under section 12AA(3) of the Act, the Director of Income-tax (Exemptions) was required to record his satisfaction that the activities of the trust were not genuine or that the activities of the trust are not being carried out in accordance with the objects of the trust. These two twin conditions would have to be satisfied before passing an order cancelling registration of the trust under section 12AA(3). He has taken us to the cancellation order as well as to the order of the Tribunal and submits that the Director of Income-tax (Exemptions) was not at all justified in invoking section 12AA(3), in cancelling the registration of the petitioner. The Tribunal had rightly interfered with the said order and therefore, no interference is called for.

16 Referring to the order passed by the Director of Income-tax (Exemptions), Mr. Dastur submits that identical grounds were given by the *DIT (Exemption)* v. *North Indian Association* [2017] 393 ITR 206 (Bom). However, this court did not accept such reasoning given by the Director as not being within the ambit of section 12AA(3).

17 His further submission is that there is a difference between cancellation of registration and non-grant of exemptions. Where receipts of a trust are hit by the proviso to section 2(15) of the Act, benefit of exemptions may not be available to the trust in assessment proceeding and income may be brought to tax, but that cannot be a ground for cancellation of registration. This was also the view of this court in *North Indian Association* (supra). He has also placed reliance on other decisions of this court, i.e., *DIT (Exemptions)* v. *Khar Gymkhana* [2016] 385 ITR 162 (Bom) ; *CIT* v. *Mumbai Metropolitan Regional Iron and Steel Market Committee* [2018] 404 ITR 171 (Bom) (Income Tax Appeal No. 43 of 2015, dated July 17, 2017) ; *CIT (Exemptions)* v. *Sadguru Narendra Maharaj Sansthan* [2018] 407 ITR 12 (Bom) and *CIT* v. *Builders Association of India* (Income Tax Appeal No. 92 of 2016, dated May 4, 2018).

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18 Responding to the submission of Mr. Kotangle that in respect of identical issue the Supreme Court has granted leave to file appeal in the Special Leave Petition filed by the Department, Mr. Dastur submits that issue in the said case is different. Referring to the decision of the Calcutta High Court from where the Department had filed SLP, i.e., *Pr. CIT* v. *JIS Foundation* [2018] 89 taxmann.com 226 (Cal), he submits that in the said case the Commissioner had cancelled registration of the assessee-trust on December 31, 2008 when sub-section (3) of section 12AA was introduced by the Finance Act, 2010 with effect from June 1, 2010. Therefore, the question for consideration before the Supreme Court is whether the Commissioner could have cancelled the registration on December 31, 2008, when the power to cancel registration was inserted in the statute book from June 1, 2010. In other words, the Commissioner had exercised a power which was not available to him on the date of exercise of power. That issue is not before the court in the present proceeding.

19 Submissions made by the learned counsel for the parties have been considered.

20 At the outset, it would be apposite to advert to the relevant provisions of the Act dealing with the trust.

21 Section 11 provides that income from property held for charitable or religious purposes shall not be included in the total income of the previous year of the person in receipt of the income.

22 Section 12 deals with income of trust or institutions from contributions. Sub-section (1) says that any voluntary contribution received by a trust created wholly for charitable or religious purposes or by an institution established wholly for such purposes shall for the purposes of section 11 be deemed to be income derived from property held under the trust wholly for charitable or religious purposes and thereafter, the provisions of sections 11 and 13 shall apply.

23 Section 12A lays down the conditions for applicability of sections 11 and 12. Before adverting to section 12AA, we may mention that section 13 provides that section 11 shall not apply in those cases mentioned in that section. Sub-section (8) of section 13 says that nothing contained in section 11 or 12 shall operate so as to exclude any income from the total income of the previous year of the person in receipt thereof if the provisions of the first proviso to clause (15) of section 2 become applicable in the case of such person in the said previous year (It may be mentioned that with effect from April 1, 2016, section 2(15) has only one proviso).

24 Section 12AA lays down the procedure for registration of a trust. Sub-sections (1), (1A) and (2) deal with the order granting or refusing

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registration and the procedure to be followed. Sub-section (3) was inserted by the Finance Act, 2004 with effect from October 1, 2004. Sub-section (3) is extracted hereunder :

> "(3) Where a trust or an institution has been granted registration under clause (b) of sub-section (1) (or has obtained registration at any time under section 12A as it stood before its amendment by the Finance (No. 2) Act, 1996 (33 of 1996) and subsequently the Principal Commissioner or Commissioner is satisfied that the activities of such trust or institution are not genuine or are not being carried out in accordance with the objects of the trust or institution, as the case may be, he shall pass an order in writing cancelling the registration of such trust or institution :
>
> Provided that no order under this sub-section shall be passed unless such trust or institution has been given a reasonable opportunity of being heard."

25 Thus where a trust or institution has been granted registration and subsequently the Principal Commissioner or Commissioner is satisfied that the activities of such trust or institution are not genuine or are not being carried out in accordance with the objects of the trust or institution, he shall pass an order in writing cancelling the registration of such trust or institution. As per the proviso no order of cancellation of registration shall be passed unless such trust or institution has been given a reasonable opportunity of being heard. Therefore, two conditions are required to be satisfied before invocation of section 12AA(3) of the Act. Firstly, the activities of the trust or institution are not genuine and secondly, the activities are not being carried out in accordance with the objects of the trust or institution. The use of the word "or" between the two conditions is indicative of the disjunctive nature of the two conditions. In other words, it is enough if one of the two conditions are satisfied. The requirement therefore is that the authority competent under section 12AA(3) to cancel registration must arrive at the satisfaction that one of the two conditions mentioned therein is attracted.

26 Before referring to the judgments cited at the Bar it would be apposite to advert to section 2(15) of the Act. As is evident section 2 is the definition section. Clause (15) defines "Charitable purpose". However, it is the proviso thereto which is relevant which existed as on the date of passing of order by the Director of Income-tax (Exemptions) on December 27, 2011. At that stage i.e., prior to April 1, 2016, there were two provisos to section 2(15) which were as under :

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"Provided that the advancement of any other object of general public utility shall not be a charitable purpose, if it involves the carrying on of any activity in the nature of trade, commerce or business, or any activity of rendering any service in relation to any trade, commerce or business, for a cess or fee or any other consideration, irrespective of the nature of use or application, or retention, of the income from such activity :

Provided further that the first proviso shall not apply if the aggregate value of the receipts from the activities referred to therein is twenty-five lakh rupees or less in the previous year."

27 Thus, as per the first proviso it was held that advancement of any other object of general public utility would not be a charitable purpose if it involved the carrying on of any activity in the nature of trade, commerce or business or any activity of rendering any service in relation to any trade, commerce or business for a cess or fee or any other consideration irrespective of the nature of use or application or retention of the income from such activity. As per the second proviso, the first proviso would not apply if the aggregate value of the receipts from such activities is Rs. 25 lakhs or less in the previous year.

28 In *North Indian Association* (supra) this court in similar circumstances observed that there is difference between registration and exemption. Referring to section 13(8) of the Act which was introduced by the Finance Act, 2012 with retrospective effect from April 1, 2009 this court held that where the receipts are hit by the proviso to section 2(15) of the Act, the benefit of exemption to its income for the relevant previous year would not be available. Thus income would be brought to tax to secure the interests of the Revenue but it does not necessarily result in automatic cancellation of registration.

29 In *Khar Gymkhana* case (supra) this court held that jurisdiction to cancel registration would only arise if there is any change in the nature of activities of the institution.

30 Having noticed the above, the objects of the respondent-trust may be adverted to. Objects of the trust appear in clause 3 of the trust deed dated July 5, 1978, which read as under :

"(i) Affording medical relief and spread of medical science in such manner as the trustees may think fit including :

(a) Establishment and maintenance and support of hospitals health centres and dispensaries with or without medical schools and nursing institutions or any of them for treatment of patients suffering from diseases or accidents.

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(b) Establishment, acquisition and maintenance and support to hospitals, dispensaries, maternity homes, homes sanatoria, research centres, laboratories. preventive health centres, hospices, diagnostic centres, medical colleges and medical schools.

(c) Grant of subscription and donation to hospitals, dispensaries, convalescent homes, asylums, hospices, health centres, baby clinics, nursing homes and other public institutions for administering medical relief upon such terms and conditions and for such period as the trustees may think fit.

(d) Grant of medical help during epidemic, famine, flood or any unforeseen calamity or war or warlike operations or civil commotion or riots.

(e) Establishment and/or acquisition and maintenance of and support of medical schools, medical colleges and other institutions carrying research in medicine and awarding scholarships and scholarship prizes or awards at any such schools, colleges and institutions.

(f) To undertake, prosecute, develop, help or carry on all or any kind of basic or fundamental and/or applied research and scientific work in connection with or relating to medical, surgical and socio-medical research problems and to do all things necessary or incidental or conducive to the attainment of the same and to provide funds for research and for scholarships, stipends and/or other payment or aid to any person or persons engaged in research work.

(g) establish and maintain and to assist and encourage or promote as and when deemed proper and expedient for the purpose of medical relief in the form of hospitals or in connection therewith or attached thereto all or any of the following institutions, namely :

(1) Institutions for promoting medical research work ;

(2) Medical college, nursery and midwifery institutions for imparting medical education and training ;

(3) Convalescent home ;

(4) Creche and children's hospital.

(2) To incur any expenditure on any programme of rural development as provided for under section 35CC of the Income-tax Act or any other law relating to rural development for the time being in force and to undertake to carry out, promote and sponsor such programme as the trustees may deem fit."

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31 We may also refer to clause 4 of the trust deed which outlines the powers vested with the trustees in order to attain the objectives of the trust. Clause 4 is as under :

> "4. The trustees shall have power to restrict or regulate from time to time the objects of this trust so as to comply with any conditions or requirements of taxation laws of India relating to taxation of income or capital as they may think fit so as to obtain for this trust or donors to this trust any relief or concession in respect of taxation subject however to the overriding consideration that the object or objects of this trust shall always be a public charitable object excluding (i.e. other than an object of a religious nature and shall be such as may be recognised as a public charitable object as defined in section 2(15) of the Income-tax Act, 1961 or any statutory modification or reenactment or any other Act governing taxation of income for the time being in force in India. Without prejudice to the generality of the foregoing object or purposes but subject to the limitation and conditions as laid down in this deed the trustees may each year spend or apply the residue of the income of the trust fund and may at their discretion at any time and from time to time spend or apply also the corpus of the trust fund or any part of parts of the trust fund in or towards any one or more of the objects or purposes (which according to law be public charitable objects or purposes) to the exclusion of the others or other of them and in such proportion and manner in all respects as the trustees may think fit."

32 In the instant case the Tribunal discussed the objects of the assessee, i.e., the respondent and returned a finding of fact that the entire objects are charitable in nature having regard to the meaning of the expression "Charitable purpose" as defined in the Act. The Tribunal referred to the decision of the Madras High Court in *Tamilnadu Cricket Association* v. *DIT (Exemptions)* [2014] 360 ITR 633 (Mad) wherein the Madras High Court held that the act of granting registration under section 12AA(1) is a result of satisfaction recorded by the Commissioner as regards genuineness of the objects as well as activities of the trust and once such a satisfaction is arrived at by the Commissioner, cancellation could only be in terms of section 12AA(3) of the Act. Thereafter, the Tribunal recorded the finding that the order of the Director of Income-tax (Exemptions) did not disclose which activity of the respondent was not genuine or that the respondent was not genuine. The Tribunal also recorded that there was no material in the said order explaining that activities of the respondent are not being carried out in accordance with its objects.

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33 On careful reading of the order passed by the Director of Income-tax (Exemptions) as well as the order passed by the Tribunal, we do not find any error or infirmity in the view taken by the Tribunal. In so far as the view taken by the Director is concerned that the respondent is directly hit by the proviso to section 2(15) of the Act, we are of the view that such satisfaction may lead to denial of exemption to the respondent in the assessment proceeding for the relevant assessment year but certainly cannot be a ground for cancellation of registration under section 12AA(3). The competent authority under section 12AA(3) must be satisfied that the activities of the trust are not genuine or that the activities are not being carried out in accordance with the objects of the trust or the institution. Such satisfaction must be recorded as a matter of fact on the basis of specific materials on record. Merely saying that the activities of the respondent is hit by the proviso to section 2(15) of the Act, would not lead to automatic cancellation of registration as that is not a ground provided under section 12AA(3) of the Act for cancellation of registration.

34 A perusal of the order passed by the Director would go to show that no such finding was recorded by the Director that the activities of the respondent-trust are not genuine or that the activities are not being carried out in accordance with the objects of the respondent-trust. What the Director had done was that he took the view that the respondent was hit by the proviso to section 2(15) of the Act and therefore, it was deemed that the respondent-trust had become non-genuine. Such a view is wholly untenable being contrary to the mandate of section 12AA(3) of the Act and was rightly interfered with by the Tribunal.

35 In so far as the contention of learned standing counsel for the Revenue that this issue is being considered by the Supreme Court, we are in agreement with the submission made by learned senior counsel for the respondent/assessee that the question before the Supreme Court is whether at the time of cancellation of registration on December 31, 2008 the Commissioner had the power to cancel registration since sub-section (3) of section 12AA was inserted by the Finance Act, 2010 with effect from June 1, 2010. Therefore, the issue in *JIS Foundation* (supra) is materially different from the issue arising in the present appeal.

36 Therefore, on thorough consideration we are of the view that there is no error or infirmity in the order passed by the Tribunal. Consequently no question of law, much less any substantial question of law, arises therefrom.

37 In that view of the matter, the appeal is dismissed. However, there shall be no order as to cost.

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THE
INCOME TAX REPORTS
VOLUME 425 — 2020
(STATUTES)

C. B. D. T. Circulars

I

Circular No. 13 of 2020, dated 13th July, 2020

Subject: **One-time relaxation for verification of tax-returns for the assessment years 2015-16, 2016-17, 2017-18, 2018-19 and 2019-20 which are pending due to non-filing of ITR-V form and processing of such returns—Reg.**

In respect of an Income-tax Return (ITR) which is filed electronically without a digital signature, the taxpayer is required to verify it using any-one of the following modes with in the time limit of 120 days from date of uploading the ITR :

(i) Through Aadhaar OTP

(ii) By logging into e-filing account through net banking

(iii) EVC through Bank Account Number

(iv) EVC through Demat Account Number

(v) EVC through Bank ATM

(vi) By sending a duly signed physical copy of ITR-V through post to the CPC, Bengaluru.

2. In this regard, it has been brought to the notice of Central Board of Direct Taxes ("CBDT") that a large number of electronically filed ITRs still remain pending with the Income-tax Department for want of receipt of a valid ITR-V Form at CPC, Bengaluru from the taxpayers concerned. In law, consequences of non-filing the ITR-V within the time allowed is significant as such a return is/can be declared non est in law, thereafter, all the consequences for non-filing a tax return, as specified in the Income-tax Act, 1961 (Act) follow.

3. In this context, as a one-time measure for resolving the grievances of the taxpayers associated with non-filing of ITR-V for earlier assessment

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years and to regularize such returns which have either become non- est or have remained pending due to non-filing/non-receipt of respective ITR-V Form, the CBDT, in exercise of powers under section 119 of the Act, *in case of returns for assessment years 2015-16, 2016-17, 2017-18, 2018-19 and 2019-20 which were uploaded electronically by the taxpayer within the time allowed under section 139 of the Act and which have remained incomplete due to non-submission of ITR-V Form for verification*, hereby permits verification of such returns either by sending a duly signed physical copy of ITR-V to CPC, Bengaluru through speed post or through EVC/OTP modes as listed in para 1 above. Such verification process must be completed by *30-9-2020*.

4. However, this relaxation shall not apply in those cases, where during the intervening period, Income-tax Department has already taken recourse to any other measure as specified in the Act for ensuring filing of tax return by the taxpayer concerned after declaring the return as non est.

5. Further, CBDT, also relaxes the time-frame for issuing the intimation as provided in second proviso to sub-section (1) of section 143 of the Act and directs that such returns shall be processed by *31-12-2020* and intimation of processing of such returns shall be sent to the taxpayer concerned as per the laid down procedure. In refund cases, while determining the interest, provision of section 244A(2) of the Act would apply.

6. In case the taxpayer concerned does not get his return regularized by furnishing a valid verification (either ITR-V or EVC/OTP) by 30-9-2020, necessary consequences as provided in law for non-filing the return may follow.

7. Hindi Version follows.

(Sd.) . . . .
Rajarajeswari R.
Under Secretary (ITA.II), CBDT
[F. No. 225/59/2020/ITA-II]

II

Circular No. 14 of 2020, dated 20th July, 2020

Subject: **Clarification in relation to notification issued under clause (v) of proviso to section 194N of the Income-tax Act, 1961 (the Act) prior to its amendment by Finance Act, 2020 (FA, 2020)—Reg.**

Section 194N of the Act as inserted by the Finance (No. 2) Act, 2019 provided for deduction of tax at source on payment made by a banking

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company, a co-operative society engaged in the business of banking or post office, in cash to a recipient exceeding Rs. 1 crore in aggregate during a financial year from one or more account maintained by such recipient. Clause (v) of proviso to the said section had empowered the Central Government, in consultation with the Reserve Bank of India (RBI), to exempt by way of notification in Official Gazette, persons or class of persons so that payments made to such persons or class of persons shall not be subjected to TDS under this section. Accordingly, in exercise of the said power, Central Government has issued three notifications which are as under :

(a) *Notification No. 68 of 2019, dated 18-9-2019*[1] : Cash Replenishment Agencies (CRAs) and franchise agents of white label automated teller machine operators (WLATMOs) for the purpose of replenishing cash in ATMs operated by these entities subject to conditions mentioned in the said notification.

(b) *Notification No. 70 of 2019, dated 20-9-2019*[2] : Commission agent or trader operating under Agriculture Produce Market Committee (APMC) and registered under any law relating to agriculture produce market of the concerned State have been exempted subject to conditions specified in the said notification.

(c) *Notification No. 80 of 2019 dated 15-10-2019*[3] *:* the authorized dealer and its franchise agent and sub-agent and Full Fledged Money Changer (FFMC) licensed by the Reserve Bank of India and its franchise agent for the purposes of,—

(i) Purchase of foreign currency from foreign tourists or non-residents visiting India or from resident Indians on their return to India, in cash as per the directions or guidelines issued by Reserve Bank of India ; or

(ii) Disbursement of inward remillances to the recipient beneficiaries in India in cash under Money Transfer Service Scheme (MFSS) of the Reserve Bank of India ;

and subject to the conditions specified in the said notification.

2. Section 194N of the Act was amended by the Finance Act, 2020 (the FA, 2020) in order to make the provisions of the said section more stringent for non-ITR filers. It is to note that the clause (v) of the proviso to section 194N prior to its amendment has now become fourth proviso to the said section. Representations have been received seeking clarification

1. See [2019] 417 ITR (St.) 54.
2. See [2019] 417 ITR (St.) 75.
3. See [2019] 418 ITR (St.) 5.

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regarding the validity of the above mentioned notifications in light of the amendments carried out by the Finance Act, 2020.

3. The matter has been examined by the Board and it is hereby clarified that the above mentioned three notifications shall be deemed to be issued under fourth proviso to section 194N as amended by the Finance Act, 2020. It is further reiterated that the exemption allowed under the said notifications shall be subject to the conditions laid down therein.

(Sd.) . . . . .
Ankit Jain,
Under Secretary (TPL)-III.
[F. No. 370142/27/2020-TPL]

Repealing and Amending Act, 2019

[No. 31 OF 2019][1]

Received the assent of the President on the 8th August, 2019.

An Act to repeal certain enactments and to amend certain other enactments.

BE it enacted by Parliament in the Seventieth Year of the Republic of India as follows :—

1. Short title.—This Act may be called the **Repealing and Amending Act, 2019**.

2. Repeal of certain enactments.—The enactments specified in the First Schedule are hereby repealed.

3. Amendment of certain enactments.—The enactments specified in the Second Schedule are hereby amended to the extent and in the manner specified in the fourth column thereof.

4. Savings.—The repeal by this Act of any enactment shall not affect any other enactment in which the repealed enactment has been applied, incorporated or referred to ;

and this Act shall not affect the validity, invalidity, effect or consequences of anything already done or suffered, or any right, title, obligation or liability already acquired, accrued or incurred, or any remedy or proceeding in respect thereof, or any release or discharge of or from any debt, penalty, obligation, liability, claim or demand, or any indemnity already granted, or the proof of any past act or thing ;

1. Gaz. of India, Extry. No. 50, dt. 8-8-2019, Pt. II, sec. 3(i).

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nor shall this Act affect any principle or rule of law, or established jurisdiction, form or course of pleading, practice or procedure, or existing usage, custom, privilege, restriction, exemption, office or appointment, notwithstanding that the same respectively may have been in any manner affirmed or recognised or derived by, in or from any enactment hereby repealed ; nor shall the repeal by this Act of any enactment revive or restore any jurisdiction, office, custom, liability, right, title, privilege, restriction, exemption, usage, practice, procedure or other matter or thing not now existing or in force.

THE FIRST SCHEDULE

(*See* section 2)

REPEALS

Year	*Act No.*	*Short Title*
1	*2*	*3*
2009	21	The Prevention of Money-laundering (Amendment) Act, 2009.
2015	21	The Companies (Amendment) Act, 2015.
2016	48	The Taxation Laws (Second Amendment) Act, 2016.

THE SECOND SCHEDULE

(*See* section 3)

AMENDMENTS

Year	*Act No.*	*Short title*	*Amendments*
1	*2*	*3*	*4*
1961	43	The Income-tax Act, 1961	In section 54GA, in the *Explanation* to sub-section (1), in clause (a), after the word, brackets, letters "clause (za)", the words and figure "of section 2" shall be inserted.

National Pension Scheme Tier II-Tax Saver Scheme, 2020

Notification No. S. O. 2232(E), dated 7th July 2020[1]*.*

In exercise of the powers conferred by clause (xxv) of sub-section (2) of section 80C of the Income-tax Act, 1961 (43 of 1961), the Central Government hereby makes the following scheme, namely :—

1. Short title and commencement.—(1) This scheme may be called the **National Pension Scheme Tier II-Tax Saver Scheme, 2020.**

1. Gaz. of India, Extry. No. 1975, dt. 7-7-2020, Pt. II, sec. 3(ii).

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(2) It shall come into force from the date of its publication in the Official Gazette.

2. Definitions.—(1) In this scheme, unless the context otherwise requires,—

(a) "Act" means the Income-tax Act, 1961 (43 of 1961) ;

(b) "authority" means the Pension Fund Regulatory and Development Authority established under sub-section (1) of section 3 of the Pension Fund Regulatory and Development Authority Act, 2013 (23 of 2013) ;

(c) "investment" means contribution in an specified account by the Central Government employee in accordance with the scheme ;

(2) The words and expressions used herein and not defined but defined in the Act shall have the same meaning as respectively, assigned to them in the Act.

3. Investment.—(i) The assessee, being a Central Government employee, shall make contribution to the specified account which has been activated by the authority in accordance with the provisions of this scheme read with the operational guidelines, if any, issued by the authority in this regard on or after the date of commencement of this scheme.

(ii) The minimum amount of contribution to activate the specified account shall be one thousand rupees and minimum amount of subsequent contribution shall be two hundred and fifty rupees.

4. Lock-in-period.—The contribution made under this scheme shall have a lock-in-period of three years from the date of credit of amount to the specified account.

5. Transferability.—The contribution made to the specified account shall not be permitted to be assigned, pledged or hypothecated during the lock-in-period.

[Notification No. 45/2020/F. No.370142/26/2019-TPL]

Income-tax (17th Amendment) Rules, 2020

Notification No. G. S. R. 464(E), dated 24th July 2020[1].

In exercise of the powers conferred by sections 197 and 206C read with section 295 of the Income-tax Act, 1961 (43 of 1961), the Central Board of Direct Taxes hereby makes the following rules further to amend the Income-tax Rules, 1962, namely :

1. Gaz. of India, Extry. No. 360, dt. 24-7-2020, Pt. II, sec. 3(i).

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1. Short title and commencement.— (1) These rules may be called the **Income-tax (17th Amendment) Rules, 2020.**

(2) Save as otherwise provided in these rules, they shall come into force with effect from the 1st day of October, 2020.

2. In the Income-tax Rules, 1962 (hereinafter referred to as the principal rules), in rule 31AA, in sub-rule (4), after clause (v), the following clauses shall be inserted namely :

"(vi) furnish particulars of amount received or debited on which tax was not collected,—

(a) by the authorised dealer from the buyer under the first proviso to sub-section (1G) of section 206C ;

(b) by the authorised dealer under the fourth proviso to sub-section (1G) of section 206C ; and

(c) by the authorised dealer or seller of an overseas tour program from the buyer under clause (i) or clause (ii) of the fifth proviso of sub-section (1G) of section 206C or in view of any notification issued under clause (ii) of the fifth proviso of sub-section (1G) of section 206C.

(vii) furnish particulars of amount received or debited on which tax was not collected from the buyer,—

(a) under the second proviso to sub-section (1H) of section 206C ; and

(b) under sub-clause (A) or sub-clause (B) or sub-clause (C), or in view of any notification issued under sub-clause (C), of clause (a) of the *Explanation* to sub-section (1H) of section 206C."

3. In the principal rules, from the date of publication in the Official Gazette, in rule 37BC, in sub-rule (1), after the words "fees for technical services", the words ", dividend" shall be inserted.

4. In the principal rules, in rule 37CA, the words, brackets, figures and letters "sub-section (1) or sub-section (1C)", wherever they occur, shall be omitted.

5. In the principal rules, in rule 37-I, after sub-rule (2), the following sub-rule shall be inserted, namely :

"(2A) Notwithstanding anything contained in sub-rule (2), for the purposes of sub- section (1F) or, sub-section (1G) or, sub-section (1H) of section 206C, credit for tax collected at source shall be given to the person from whose account tax is collected and paid to the Central Government account for the assessment year relevant to the previous year in which such tax collection is made."

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6. In the principal rules, in Appendix II, in Form 27EQ, for the "Annexure", the following "Annexure" shall be substituted, namely :—

"ANNEXURE : *Party wise break up of TCS*

(Please use separate Annexure for each-line item in Table at Sl. No. 04 of main Form 27EQ)

Details of amount received/debited during the quarter ended . . . . (dd/mm/yyyy) and of tax collected at source

BSR Code of branch/Receipt Number of Form No. 24G		Name of the Collector	
Date on which challan deposited/Transfer voucher date (dd/mm/yyyy)		TAN	
Challan Serial Number/DDO Serial No. of Form No. 24G			
Amount as per Challan			
Total TCS to be allocated among deductees as in the vertical total of Col. 677			
Total interest to be allocated among the parties mentioned below			

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Sl. No.	*Party reference number provided by the collector, if available*	*Party code (01-Company 02-Other than company)*	*PAN of the party*	*Name of party*	*Total value of the transaction*	*Amount received/ debited*	*Date on which amount received/ debited (dd/mm/ yyyy)*	*Collection Code (See Note 9)*	*Tax*	*Surcharge*	*Education Cess*	*Total tax collected [673+ 674+675]*	*Total tax deposited*	*Date of collection (dd/ mm/yy yy)*	*Rate at which collected*	*Reason for non-collection/ lower collection/or collection at higher rate (See Note 1 to 8)*	*Number of the certificate under section 206C issued by the Assessing Officer for lower collection of tax*	*Whether the payment by collectee is liable to TDS as per clause (a) of the fifth proviso to sub-section (1G) or second proviso to sub-section (1H) and whether TDS has been deducted from such payment (if either "F" or "G" is selected in 680)*	*If, answer to [681A] is yes, then*	
																			Challan number	*Date of payment of TDS to Central Government*
[664]	*[665]*	*[666]*	*[667]*	*[668]*	*[669]*	*[670]*	*[671]*	*[672]*	*[673]*	*[674]*	*[675]*	*[676]*	*[677]*	*[678]*	*[679]*	*[680]*	*[681]*	*[681A]*	*[681B]*	*[681C]*
1																				
2																				
3																				
Total																				

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Verification

I, ..., hereby certify that all the particulars furnished above are correct and complete.

Place : . . . . Signature of the person responsible for collecting tax at source

Date : . . . . Name and designation of the person responsible for collecting tax at source.

Notes :

1. Write "A" if "lower collection" is on account of a certificate under sub-section (9) of section 206C.
2. Write "B" if "non-collection" is on account of furnishing of declaration under sub-section (1A) of section 206C.
3. Write "C" if collection is at higher rate on account of non-furnishing of PAN/Aadhaar by the collectee.
4. Write "D" if no collection is on account of the first proviso to sub-section (1G) of section 206C.
5. Write "E" if no collection is on account of the fourth proviso to sub-section (1G) of section 206C.
6. Write "F" if no collection is on account clause (i) or clause (ii) of the fifth proviso to sub-section (1G) or in view of notification issued under clause (ii).
7. Write "G" if no collection is on account of the second proviso to sub-section (IH) of section 206C.
8. Write "H" if no collection is on account of sub-clause (A) or sub-clause (B) or sub-clause (C), or in view of notification issued under sub-clause (c), of clause (a) of the *Explanation*.
9. Write collection code as mentioned below :

Section	*Nature of collection*	*Collection*	*Code*
206C	Collection at source from alcoholic liquor for human consumption	6C	A
206C	Collection at source from timber obtained under forest lease	6C	B
206C	Collection at source from timber obtained by any mode other than a forest lease	6C	C
206C	Collection at source from any other forest produce (not being tendu leaves)	6C	D
206C	Collection at source from scrap	6C	E

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206C	Collection at source from contractors or licensee or lease relating to parking lots	6C	F
206C	Collection at source from contractors or licensee or lease relating to toll plaza	6C	G
206C	Collection at source from contractors or licensee or lease relating to mine or quarry	6C	H
206C	Collection at source from tendu leaves	6C	I
206C	Collection at source on sale of minerals, being coal or lignite or iron ore	6C	J
206C	Collection at source on cash sale of bullion and jewellery	6C	K
206C	Collection at source on sale of motor vehicle	6C	L
206C	Collection at source on remittance under LRS for purchase of overseas tour program package	6C	O
206C	Collection at source on remittance under LRS for educational loan taken from financial institution mentioned in section 80E	6C	P
206C	Collection at source on remittance under LRS for purpose other than for purchase of overseas tour package or for educational loan taken from financial institution	6C	Q
206C	Collection at source on sale of goods	6C	R"

[Notification No. 54/2020/F. No. 370142/22/2020-TPL]

Income-tax Act, 1961 : Notification under section 10(46) : Exemption to Board/Trust/Commission/Authority/Society constituted with object of regulating/administering an activity for benefit of general public

I

Notification No. S. O. 1188(E), dated 20th March, 2020[1].

In exercise of the powers conferred by clause (46) of section 10 of the Income-tax Act, 1961 (43 of 1961), the Central Government hereby makes the following amendments in the notification of the Government of India, Ministry of Finance, (Department of Revenue), (Central Board of Direct Taxes) number S. O. 1537(E), dated 9th April, 2019[2] published in the Gazette of India, Extraordinary, Part II, section 3, sub-section (ii), namely :—

2. In the said notification,—

1. Gaz. of India, Extry. No. 1060, dt. 20-3-2020, Pt. II, sec. 3(ii).
2. See [2019] 413 ITR (St.) 10.

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(a) for the third paragraph, the following paragraph shall be substituted, namely :—

"3. This notification shall be deemed to have been applied for the period from 1-6-2011 to 31-3-2012 in the assessment year of 2012-2013 and also from the assessment years 2013-2014, 2014-2015, 2015-2016, 2016-2017, 2017-2018, 2018-2019 and shall apply with respect to the assessment years 2019-2020, 2020-2021, 2021-2022, 2022-2023 and 2023-2024." ;

(b) at the end, the following Explanatory Memorandum shall be inserted, namely :—

"Explanatory Memorandum

This notification shall be given retrospective effect for the period from 1-6-2011 to 31-3-2012 in the assessment year of 2012-2013 and also from the assessment years 2013-2014, 2014-2015, 2015-2016, 2016-2017, 2017-2018, 2018-2019, in view of the order of the hon'ble High Court of Karnataka in the matter of *Mysore Palace Board* v. *CBDT* (W. P. No. 40801 of 2019 (T-IT)), dated 17th day of December, 2019[1]. It is certified that by giving retrospective effect to the notification no person interest will adversely get affected.".

3. This notification shall be deemed to have come into effect from 9th April, 2019.

[Notification No. 19/2020/F. No. 300196/63/2018-ITA-I]]

Explanatory Memorandum

It is hereby certified that no person interest is adversely affected by giving retrospective effect to this notification from 9th April, 2019.

II

Notification No. S. O. 2326(E), dated 13th July 2020[2].

In exercise of the powers conferred by clause (46) of section 10 of the Income-tax Act, 1961 (43 of 1961), the Central Government hereby notifies for the purposes of the said clause, "National Aviation Security Fee Trust" (PAN AADTN2508F), a trust established by the Central Government, in respect of the following specified income arising to that trust, namely :

(a) Grant or subsidy or any receipt in the nature of grant as approved by/under directions of Ministry of Civil Aviation, Government of India ;

1. See [2019] 413 ITR (St.) 10.
2. Gaz. of India, Extry. No. 2052, dt. 14-7-2020, Pt. II, sec. 3(ii).

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(b) Aviation Security Fee collected at the prevailing rates as per orders of Ministry of Civil Aviation, Government of India ;

(c) Amount transferred from escrow accounts for deposits of the passenger service fee (security component) maintained by airport operators with the scheduled banks for Ministry of Civil Aviation, Government of India as beneficiary ; and

(d) Interest/Dividend earned on investment of amount collected if it is utilized to meet expenditure to realize objectives of the trust.

2. This notification shall be effective subject to the conditions that National Aviation Security Fee Trust,—

(a) shall not engage in any commercial activity ;

(b) activities and the nature of the specified income shall remain unchanged throughout the financial years ; and

(c) shall file return of income in accordance with the provision of clause (g) of sub-section (4C) of section 139 of the Income-tax Act, 1961.

(d) shall file the audit report along with the Return, duly verified by the accountant as provided in *Explanation* to section 288(2) of the Income-tax Act, 1961 along with a certificate from the chartered accountant that the above conditions are satisfied.

3. This notification shall apply with respect to the assessment years 2020-21, 2021-22, 2022-23, 2023-24 and 2024-25.

[Notification No. 46/2020/F. No. 300196/07/2020-ITA-I]

III

Notification No. S. O. 2327(E), dated 13th July 2020[1].

In exercise of the powers conferred by clause (46) of section 10 of the Income-tax Act, 1961 (43 of 1961), the Central Government hereby notifies for the purposes of the said clause, "Real Estate Regulatory Authority" as specified in the schedule to this notification, constituted by the Government in exercise of powers conferred under sub-section (1) of section 20 of the Real Estate (Regulation and Development) Act, 2016 (16 of 2016) as a "class of Authority" in respect of the following specified income arising to that Authority, namely :

(a) Amount received as Grants-in-aid or loan/advance from Government ;

1. Gaz. of India, Extry. No. 2053, dt. 14-7-2020, Pt. II, sec. 3(ii).

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(b) Fee/penalty received from builders/developers, agents or any other stakeholders as per the provisions of the Real Estate (Regulation and Development) Act, 2016 ;

(c) Interest earned on (a) and (b) above.

2. This notification shall be effective subject to the conditions that each of the Real Estate Regulatory Authority,—

(a) shall not engage in any commercial activity ;

(b) activities and the nature of the specified income shall remain unchanged throughout the financial years ; and

(c) shall file return of income in accordance with the provision of clause (g) of sub-section (4C) of section 139 of the Income-tax Act, 1961.

(d) shall file the audit report along with the Return, duly verified by the accountant as provided in *Explanation* to section 288(2) of the Income-tax Act, 1961 along with a certificate from the chartered accountant that the above conditions are satisfied.

3. This notification shall apply to the Real Estate Regulatory Authority, mentioned at column (2) below, with respect to the assessment years mentioned in column (4) below.

SCHEDULE

Sl. No.	*Name of the Real Estate Regulatory Authority*	*PAN*	*Assessment years*
(1)	*(2)*	*(3)*	*(4)*
1.	Goa Real Estate Regulatory Authority	AAAGG3912L	2019-2020, 2020-2021, 2021-2022, 2022-2023, 2023-2024
2.	Telangana State Real Estate Regulatory Authority	AAAGT0709A	2019-2020, 2020-2021, 2021-2022, 2022-2023, 2023-2024

[Notification No. 47/2020/F. No. 300196/13/2019-ITA-I]

IV

Notification No. S. O. 2380(E), dated 17th July 2020[1].

In exercise of the powers conferred by clause (46) of section 10 of the Income-tax Act, 1961 (43 of 1961), the Central Government hereby notifies for the purposes of the said clause, "Real Estate Regulatory Authority" as specified in the schedule to this notification, constituted by the Government in exercise of powers conferred under sub-section (1) of section 20 of the Real Estate (Regulation and Development) Act, 2016 (16 of 2016) as a

1. Gaz. of India, Extry. No. 2097, dt. 17-7-2020, Pt. II, sec. 3(ii).

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"class of Authority" in respect of the following specified income arising to that Authority, namely :—

(a) Amount received as Grants-in-aid or loan/advance from Government ;

(b) Fee/penalty received from builders/developers, agents or any other stakeholders as per the provisions of the Real Estate (Regulation and Development) Act, 2016 ; and

(c) Interest earned on (a) and (b) above.

2. This notification shall be effective subject to the conditions that each of the Real Estate Regulatory Authority,—

(a) shall not engage in any commercial activity ;

(b) activities and the nature of the specified income shall remain unchanged throughout the financial years ;

(c) shall file return of income in accordance with the provision of clause (g) of sub-section (4C) of section 139 of the Income-tax Act, 1961 ; and

(d) shall file the audit report along with the Return, duly verified by the accountant as provided in *Explanation* to section 288(2) of the Income-tax Act, 1961 along with a certificate from the chartered accountant that the above conditions are satisfied.

3. This notification shall apply to the Real Estate Regulatory Authority, mentioned at column (2) below, with respect to the assessment years mentioned in column (4) below.

SCHEDULE

Sl. No.	*Name of the Real Estate Regulatory Authority*	*PAN*	*Assessment years*
(1)	*(2)*	*(3)*	*(4)*
1.	Real Estate Regulatory Authority, Bihar	AAAGR1030C	2020-2021, 2021-2022, 2022-2023, 2023-2024 and 2024-2025

[Notification No. 49/2020/F. No. 300196/43/2019-ITA-I]

V

Notification No. S. O. 2403(E), dated 21st July 2020[1].

In exercise of the powers conferred by clause (46) of section 10 of the Income-tax Act, 1961 (43 of 1961), the Central Government hereby notifies for the purposes of the said clause, "Tamil Nadu e-Governance Agency",

1. Gaz. of India, Extry. No. 2118, dt. 21-7-2020, Pt. II, sec. 3(ii).

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an agency formed by the State Government of Tamil Nadu, in respect of the following specified income arising to that Authority, namely :

(a) Amount received in the form of recurring contributions/Grants-in-aid from Governments including Government of Tamil Nadu and specified authorities, if any, towards current operational expenditure ;

(b) Service charges received through Common Service Centre's for offering online services to citizens ;

(c) Service charges for the software development projects and IT consultancies rendered for other State Government Departments/Public Sector Undertakings/Statutory Boards and interest earned on sources of funds received in advance, pending disbursements, from time to time towards various projects sponsored ;

(d) Dividend received from CSC e-Governance Services India Limited (CSC-SPV) ;

(e) Admin cost on PEC grants released by UIDAI to enrolment agencies through Tamil Nadu e-Governance Agency which is functioning as enrolment Registrar ;

(f) Revenue sharing on conducting online examination for other State Government Departments/Public Sector Undertakings/Statutory Boards ;

(g) Any other income that may arise in future incidental to/furtherance of the objects of the society ; and

(h) Interest earned on (a) to (g) above.

2. This notification shall be effective subject to the conditions that Tamil Nadu e-Governance Agency, Chennai Authority,—

(a) shall not engage in any commercial activity ;

(b) activities and the nature of the specified income shall remain unchanged throughout the financial years ;

(c) shall file return of income in accordance with the provision of clause (g) of sub-section (4C) of section 139 of the Income-tax Act, 1961 ; and

(d) shall file the audit report along with the Return, duly verified by the accountant as provided in *Explanation* to section 288(2) of the Income-tax Act, 1961 along with a certificate from the chartered accountant that the above conditions are satisfied.

3. This notification shall be deemed to have been applied for the assessment year 2019-2020 and shall apply with respect to the assessment years 2020-2021, 2021-2022, 2022-2023 and 2023-2024.

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