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IN THE INCOME TAX APPELLATE TRIBUNAL
AGRA BENCH, AGRA

BEFORE SHRI R.K. GUPTA, JUDICIAL MEMBER AND
SHRI P.K. BANSAL, ACCOUNTANT MEMBER

ITA No.110/Agr./2006
Asst. Year: 2001-02

Shiva Automobiles, (Auto Division), G.T. Road, Aligarh. (PAN : AADFS 4944 G) (Appellant)	Vs.	Income-tax Officer, Ward 1A, Aligarh. (Respondent)

Appellant by : Shri Sahib P. Satsangee, C.A.
Respondent by: Shri S.R. Sahu, Jr. D.R.

ORDER

PER P.K. BANSAL, A.M.:

In this case the difference arose between the Members of the Division Bench hearing this appeal. Therefore, the matter was referred to the opinion of the ld. Third Member. The ld. Third Member has agreed with the view of the ld. Accountant Member. Therefore, in view of the majority decision, the assessee's appeal is partly allowed.

2. In the result, appeal of the assessee is treated as allowed in part.

(Order pronounced in the open Court on 13.04.2010).

Sd/- **(R.K. GUPTA)** Judicial Member	Sd/- **(P.K. BANSAL)** Accountant Member

Place: Agra
Date: 13th April, 2010.

PBN/*

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3. CIT concerned
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(AS THIRD MEMBER)

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Shiva Automobiles, (Auto Division), G.T. Road, Aligarh. (PAN : AADFS 4944 G) (Appellant)	Vs.	Income-tax Officer, Ward 1A, Aligarh. (Respondent)

Appellant by : Shri Sahib P. Satsangee, C.A.
Respondent by: Shri Deepak Tiwari, Sr. D.R.

ORDER

This appeal came before me as a Third Member to express my opinion on the following question :-

"Whether, in the given facts and the circumstances of this case, the assessment order in question, is not erroneous, in so far as it is prejudicial to the interests of the Revenue or it is partly so ?"

2. The brief facts of the case are given in the detailed orders of my ld. Brothers. Yet, for the disposal of this case, it is necessary for me to restate the facts in brief.

3. The assessment in the case of the assessee was completed under section 143(3) of the Income-tax Act, 1961 ('the Act' hereinafter) vide order dated 29.08.2003, assessing the income of the assessee at Rs.91,240/-. In the assessment order, salary and interest to the partners was allowed at Rs.1,22,646/- and Rs.32,685/- respectively and the assessee was assessed in the status of a firm. Subsequently, the C.I.T. issued show cause notice under section 263 of the Act to the assessee on 09.03.2006 requiring him to show cause as to why the assessment order dated

29.08.2003 may not be set aside by invoking the provisions of section 263 of the Act on the following points :-

> *"While going through the case records, it has been noticed that the assessee had made entries in the partner's capital account represented by credits otherwise than credit of money, i.e. transfer of shares held in the name of partners by book entry without the shares having been transferred in the name of the firm. The implication is that interest allowed to the partners on the capital in respect of such credits is not admissible as a deduction within the meaning of section 36(1)(iii). The assessee deals in the business of automobiles and does not deal in shares. Moreover, the dividend income from shares so transferred to the firm by way of book entry has been enjoyed by the partners. Even though the said income is exempt u/s 10(33) in the hands of any holder, nevertheless it amounts to sharing the profits otherwise than in accordance with the partnership deed and accordingly, the firm should have been assessed in the status of AOP with the maximum marginal rate of tax after disallowing both salary and interest amounting to Rs.1,22,646/- and Rs.32,685/- respectively.*

4. Against this notice, the assessee submitted reply to the C.I.T. vide his submissions dated 27.03.2006 and 29.03.2006. The main contentions of the assessee was that the order passed by the A.O. on 29.08.2003 under section 143(3) is not erroneous because the provisions of section 185 can be applied only when the assessee does not fulfill the provisions of section 184 of the Act which are as under :-

- i) The partnership deed is evidenced by an instrument;
- ii) The individual shares of the partners are specified in that instrument;
- iii) Certified copy of the partnership deed is filed.

5. Since the assessee complied with all the conditions, the assessee has to be assessed as a firm and not as AOP under section 185 of the Act. As per section 184(3), once the firm is assessed as a firm for any Assessment Year, it shall be assessed in the same capacity for every subsequent year, if there is no change in the constitution of the firm or the shares of the partners. The firm is assessed to tax as partnership firm since 01.04.1998. Therefore, the question of

assessing the assessee as AOP does not arise. It was also submitted that there is no bar in the Partnership Act to transfer the assets from the partners to the firm or vice versa. The credit entries made in the capital account of the partner represented genuine transaction and do not violate the terms of the partnership deed as well as the provisions of section 184 of the Act. The payment of interest was made in accordance with the provisions of section 40(b) of the Act. The provisions of section 14A cannot be applied, as the income from trading of the shares is not totally exempt. Only a part of the income earned as dividend is exempt. As per proviso to section 14A, the A.O. has no power to reassess or rectify the assessment for disallowing the interest. The C.I.T. after considering the submissions of the assessee came to the view that the issue under consideration is not concerned with the transfer of the shares from partners to the firm, but the same is concerned with the distribution of profits from dividend/shares, in accordance with the partnership deed. It was observed that the assessee filed partnership deed and the assessee was assessed as a firm since 01.04.1998, but according to the C.I.T. if the partnership deed is not being followed in practical sense, the same becomes merely a written instrument, having no legal sanctity whatsoever. He referred to the decision of Rajasthan High Court in the case of Bheru Ram Ratan Lal vs. CIT, 257 ITR 795 in which it was held that the partners must have acted as per the terms of the partnership deed to arrive at the conclusion that the firm is genuine. According to the C.I.T., since the dividend derived from the shares did not appear in the books of accounts of the assessee and there is no evidence to show that the same is distributed amongst the partners as per the provisions of partnership deed, the A.O. failed to investigate this issue and, therefore, ultimately the C.I.T. concluded that the order passed by the A.O. on 29.08.2003 was erroneous in so far as prejudicial to the interest of the Revenue. Accordingly, he set aside the assessment order with the directions that the A.O. shall make enquiries about the genuineness of the provisions contained in section 184 and 185 of the Act. If

the profit of the firm has not been distributed in accordance with the partnership deed, the firm has to be assessed as per the provisions of section 185. It was further directed that the A.O. should see that the expenses including interest against exempt income are not allowed. The assessee came in appeal against the order of C.I.T. before the Tribunal. The ld. Judicial Member (J.M.) set aside the order passed under section 263 by the C.I.T. His reasoning as given are as under :-

i) There is no evidence that the dividends were actually received on shares and the same were distributed amongst the partners otherwise than as per the provisions of the partnership deed.

ii) Revisional powers under section 263 of the Act cannot be enlarged for reopening of the assessment proceedings which were concluded earlier only on flimsy grounds.

iii) C.I.T. has to have in his possession material on record to arrive at satisfaction. The A.O. has to exercise the quasi judicial power vested in him and if he exercises the said power in accordance with law and arrive at a conclusion, such conclusion cannot be termed to be erroneous simply because the Commissioner does not feel satisfied with the conclusion. Thus, the order of the A.O. was held not to be termed as erroneous as far as the facts qua grounds of dividend shares is concerned.

iv) In respect to the second point taken by the C.I.T. that he is satisfied that the provisions of section 14A are not being invoked at all, in that eventuality interest against dividend income becomes allowable if no dividend is received as per the decision of Hon'ble Apex Court in the case of CIT vs. Raghunandan Prasad Mody, 115 ITR 519 (SC) and that of CIT vs. Indian Bank Limited reported in 56 ITR 77 (SC).

v) The decision of C.I.T. is based on presumption, as there is no evidence on record before the C.I.T. that any expenses other than interest to partners against exempted income was allowed.

vi) The C.I.T. himself admitted that provisions of section 14A are not being invoked at all and when the provisions of section 14A are not invoked, the decision of Hon'ble Supreme Court in the case of CIT vs. Raghunandan Prasad Modi (supra) would apply and the interest paid on purchase of shares will be allowed even if no dividend is received.

6. Ld. Accountant Member (A.M.) did not agree with the order proposed by the ld. J.M. in his dissenting order. Reasoning given in his dissenting order states as under :-

i) That no enquiry in the matter stood made by the A.O. and, therefore, his order suffers from an inherent lack of application of mind in framing the assessment.

ii) He was of the opinion that this is clear and settled position of law laid down under section 263 of the Act in view of the following decisions of the Hon'ble Supreme Court :-

   a) Rampyari Devia Sarogi vs. CIT, 67 ITR 84 (SC)
   b) Tara Devi Agarwal vs. CIT, 88 ITR 323 (SC)

iii) He also referred to the decision of Hon'ble Delhi High Court in the case of Gee Vee Enterprises vs. Addl. CIT, 99 ITR 375 (Delhi) for the proposition that an order passed without due enquiry is per se erroneous in so far as it is prejudicial to the interest of the Revenue.

iv) There was no application of mind in the matter on the part of the A.O. which he statutorily bound to undertake so that assessment could be framed in accordance with law. He was of the opinion that the fact of no enquiry in this case on the stated issue was undisputed and, therefore, C.I.T. has rightly invoked the provisions of section 263 of the Act. It was also observed that when the firm's capital stands invested in shares, to that extent it couldn't be said to be utilized or applied for the purpose of business of the assessee. Therefore, interest thereon which stands allowed to the partners does not qualify for deduction under section 36(1)(iii) subject to the conditions specified in section 40(b). Non-application of section 14A is not the issue, the same were otherwise applicable being precluded for invocation by proviso to section itself. The assessee nowhere claims that the shares were acquired for the purpose of business. Even if this contention was raised, this should have been supported by material and the explanation subject to the verification by the A.O. What constitutes business, as the assessee has not been engaged in trading of the shares, is investment in shares cannot be regarded to be a business unless it is exhibited to be part of the firm's investment programme.

v) The second issue on which the assessment was set aside by the C.I.T. is the non-compliance of the provisions of section 184, and consequently, application of section 185. This is also un-arguable as to the extent the dividend stands received on the shares that the firm's property directly by the partners without being routed through the firm's accounts, the allocation of the firm's profit would not be in accordance with the provisions of the partnership deed.

vi) The provisions of section 184(3) cannot be detracted from the provisions of the partnership law which governs the partnership exchanged either in partners or in their shares stands envisaged and dealt with under section 187 of the Act. Non-receipt of the dividend is purely incidental and decide the issue. If there is any dividend, it has to be

through the assessee's Profit & Loss account and will be subject to the verification by the A.O. in the set aside proceedings.

7. Thus, the ld. A.M. confirmed the action of C.I.T. on the basis of non-conduction of enquiry by the A.O. while framing the assessment.

8. I have heard both the parties in this case. The ld. A.R. supported the order of the ld. J.M. whereas the ld. D.R. supported the order of the ld. A.M. as also of the Revenue authorities. Ld. A.R. before us pointed out that the show cause notice under section 263 was issued in respect of the following issues:-

a) Interest allowed to the partners on the capital in respect of credit entries for transfer of shares is not admissible as a deduction within the meaning of section 36(1)(iii)

b) Dividend income from shares so transferred has been enjoyed by the partners, which amounts to sharing of profits otherwise than in accordance with the partnership deed and accordingly the firm should have been assessed in the status of AOP.

c) The CIT held that the assessment dated 29.08.2003 is erroneous as well as prejudicial to the interest of Revenue on the following two grounds :-

    1) The dividends from sharers is not appearing in the books of accounts of the assessee and there is no evidence to show that the same is being distributed amongst the partners as per the provisions of the partnership deed and the A.O. has failed to investigate this issue.

    2) The interest against the dividend income is not allowable and the A.O. has failed to look into this aspect.

9. Thus, it was contended that grounds in the order passed under section 263 are different from the grounds on the basis of which the notice under section 263 was issued. The revisional order based on the ground different from stated in the notice is invalid.

10. It was also pointed out that no material on record being brought which may prove that total non-application of mind on the part of the A.O. or the A.O. has committed glaring mistake

of law or fact. The jurisdiction under section 263 of the Act cannot be utilized as an instrument for reopening the concluded proceedings on flimsy grounds or on assumption. Reliance was placed in this regard on the decision of Mrs. Khatiza S. Oomerbhoy vs. ITO, 100 ITD 173 (Mum.). Section 36(1)(iii) of the Act pertains to allowability of interest on borrowed capital, while the allowability of the interest on capital of partners is further subject to the provisions of section 40(b) read with section 184 of the Act. As far as the issue that dividend income from shares so transferred has been enjoyed by the partners, which amounts to sharing of profit otherwise than in accordance with partnership deed and accordingly the firm should have been assessed in the status of AOP, is concerned, it is most respectfully stated that according to section 184, a firm shall be assessed as a firm for the purpose of Income-tax Act if the partnership is evidenced by an instrument; the individual shares of the partners are specific in that instrument; and certified copies of the partnership deed is filed. The assessee fulfilled all the three conditions and, therefore, has to be assessed as a firm and not as AOP. Again it was pointed out that the provisions of section 184(3) are not applicable as there is no change in the constitution of the firm or shares of the partners. The assessee is assessed as partnership firm since 01.04.1998. The no evidence with C.I.T. that the dividends were actually received on shares and that the same have been distributed to the partners otherwise than as per the provisions of partnership deed, the Commissioner must have the material on record to arrive at a satisfaction that the dividends received on the shares have not been recorded in the books of the assessee. If the A.O. has taken one of the view in accordance with the law, the conclusion arrived at by the A.O. cannot be disturbed if the C.I.T. is not satisfied with the view of A.O. The C.I.T. has stated that the provisions of the section 14A are not being invoked at all. When the provisions of section 14A is not invoked, interest against dividend income is allowable even if no dividend is received as per the decision of the Apex Court in the case of CIT vs. Raghunandan

Prasad Mody, 115 ITR 519 (SC) and also the decision in the case of CIT vs. Indian Bank Limited reported in 56 ITR 77 (SC) and, therefore, the order of the A.O. cannot be regarded to be erroneous. Further the order is not prejudicial to the interest of the Revenue because the same pertains to dividend income that is exempt. He invited our attention to the terms and conditions of the partnership deed appearing at page no. 47 of the Paper Book and pointed out that the business of the partnership firm is and shall be that of purchase and sale of scooters and auto parts or such any other business or businesses as the partners may mutually decide from time to time. Referring to clause (8) of the partnership deed, it was contended that whenever capital is required for the purpose of business, it shall be contributed by the partners in such manner as is mutually agreed upon amongst the partners from time to time and the partners are entitled for the simple interest @ 18% per annum as may be prescribed under section 40(b) on their capital, current or loan account. Referring to page 56 of the paper Book, it was pointed out that the partners have contributed capital by way of transferring the shares to the firm and they have withdrawn the capital by taking off the shares. Referring to page 59 of the Paper Book, it was pointed out that the shares were duly shown in the balance sheet of the partnership firm under schedule-VI. There is no embargo in partnership deed for the purchase and sale of the shares. Referring to Assessment Order, which was set aside by the C.I.T., appearing at pages 23 to 27 of the Paper Book, it was pointed out that the assessee has duly produced all the books of accounts including the balance sheet which were duly examined by the A.O. Even the capital account was also duly looked into by the A.O. It was pointed out that the subsequent order passed after the impugned order under section 263 is available at pages 104 to 106 of the Paper Book. He also referred, during the course of the arguments, the following decisions:-

CIT Vs. Max India Ltd., 295 ITR 282 (SC).
Malabar Industrial Co. Vs. CIT, 243 ITR 83 (SC).
CIT Vs. Arvind Jewellers, 259 ITR 502 (Guj).

11. Ld. D.R., on the other hand, pointed out that for the issue as has been pointed out by the C.I.T. in the order framed under section 263 has not been looked into or examined by the A.O, it is a case of total failure on the part of the A.O. not to look into on the receipt of the dividend income on the shares and also the fact that the interest against dividend income was not allowable. It is a fact that the A.O. has assessed in subsequent assessment the assessee as a firm and not as A.O.P. and this issue is also not before the Third Member. The question referred to Third Member only related to, whether the order passed under section 263 of the Act is erroneous in so far as it is prejudicial to the interest of the Revenue. Lack of total inquiry on the part of the A.O. tantamount to that the order passed by A.O. is erroneous. He vehemently supported the order of the Ld. AM.

12. I have carefully considered the rival submissions alongwith the materials on record and the case laws relied on before me. In this case, it is not disputed fact that the assessee has claimed deduction u/s 36(1)(iii) read with section 40b in respect of interest paid on the capital of the partners. This is also a fact on record that the assessee firm got the shares transferred in its books of account standing the name of its partners by crediting their respective capital account in the ratio, the shares are owned and transferred by each of them to the firm respectively. This is also an admitted fact that the dividend received on these shares has not been accounted for in the books of account of the firm and has been received by the partner, if distributed by the respective companies, in whose name the shares stand and partners has not given the account of the dividend income relating to the shares brought in the firm. The capital account of the partners since credited by the shares so transferred into the firm, the partners were allowed interest on the capital so increased due to this credit.

13. The CIT invoked jurisdiction u/s 263 of the Act and issued show cause notice to the assessee on the following points for which the Assessing Officer ought to have made enquiries:

> *"While going through the case records, it has been noticed that the assessee had made entries in the partner's capital account represented by credits otherwise than credit of money, i.e. transfer of shares held in the name of partners by book entry without the shares having been transferred in the name of the firm. The implication is that interest allowed to the partners on the capital in respect of such credits is not admissible as a deduction within the meaning of section 36(1)(iii). The assessee deals in the business of automobiles and does not deal in shares. Moreover, the dividend income from shares so transferred to the firm by way of book entry has been enjoyed by the partners. Even though the said income is exempt u/s 10(33) in the hands of any holder, nevertheless it amounts to sharing the profits otherwise than in accordance with the partnership deed and accordingly, the firm should have been assessed in the status of AOP with the maximum marginal rate of tax after disallowing both salary and interest amounting to Rs.1,22,646/- and Rs.32,685/- respectively.*

14. Thus, the CIT was of the view that there is the failure on the part of the Assessing Officer to make the enquiry and accordingly he set aside the assessment as per the conclusion given under para 6 of his order. Section 263 of the Act lays down as under:

> *"263. (1) The Commissioner may call for and examine the record of any proceeding under this Act, and if he considers that any order passed therein by the Assessing Officer is erroneous insofar as it is prejudicial to the interests of the revenue, he may, after giving the assessee an opportunity of being heard and after making or causing to be made such inquiry as he deems necessary, pass such order thereon as the circumstances of the case justify, including an order enhancing or modifying the assessment, or cancelling the assessment and directing a fresh assessment.*
>
> > *Explanation.-For the removal of doubts, it is hereby declared that, for the purposes of this sub-section, -*
> >
> > > *(a) an order passed on or before or after the 1st day of June, 1988 by the Assessing Officer shall include -*
> > >
> > > > *(i) an order of assessment made by the Assistant Commissioner or Deputy Director or the Income-tax Officer on the basis of the directions issued by the Joint Commissioner under section 144A;*

(ii) an order made by the Joint Commissioner in exercise of the power or in the performance of the functions of an Assessing Officer conferred on, or assigned to, him under the orders or directions issued by the Board or by the Chief Commissioner or Director General or Commissioner authorised by the Board in this behalf under section 120;

(b) "record" shall include and shall be deemed always to have included all records relating to any proceeding under this Act available at the time of examination by the Commissioner;

(c) where any order referred to in this sub-section and passed by the Assessing Officer had been the subject matter of any appeal filed on or before or after the 1st day of June, 1988, the powers of the Commissioner under this sub-section shall extend and shall be deemed always to have extended to such matters as had not been considered and decided in such appeal.

(2) No order shall be made under sub-section (1) after the expiry of two years from the end of the financial year in which the order sought to be revised was passed.

(3) Notwithstanding anything contained in sub-section (2), an order in revision under this section may be passed at any time in the case of an order which has been passed in consequence of or to give effect to, any finding or direction contained in an order of the Appellate Tribunal, the High Court or the Supreme Court.

Explanation.-In computing the period of limitation for the purposes of sub-section (2), the time taken in giving an opportunity to the assessee to be reheard under the proviso to section 129 and any period during which any proceeding under this section is stayed by an order or injunction of any court shall be excluded."

15. From the perusal of the aforesaid section, it is apparent that there are four main features of the power of revision to be exercised u/s 263 by the Commissioner of Income-tax. Firstly, the Commissioner may call for and examine the records of any proceedings under the Act and for this purpose he need not to show any reason or record any reason to believe. It is a part of his administrative power to call for the record and examine them relating to any assessee. Secondly, he may consider any order passed by the Assessing Officer as erroneous as well as prejudicial to the interest of the Revenue. This consideration having regard to the language of section 263 apparently is a consideration which he exercises by calling for and examining the record

available at this stage. There is no question of the assessee to appear and make submission. Thirdly, if after calling for and examining the records the Commissioner considers that the order of the Assessing Officer is erroneous in so far it is prejudicial to the interest of the Revenue, he is bound to give an opportunity to the assessee of being heard and after making or causing to be made such enquiry as he may deem fit, pass such order thereon as the circumstances of the case may justify including an order enhancing or modifying the assessment or canceling assessment and directing a fresh assessment. This empowers the C.I.T. to cause or make such enquiries as he deems necessary. Fourthly, the C.I.T. u/s 263 can enhance or modify the assessment.

16. Thus, it is apparently clear that in order to invoke the provisions of section 263, both the conditions that the order passed by the AO is erroneous and also that it is prejudicial to the interest of Revenue must be satisfied. If one of them is absent, the provisions of section 263 cannot be invoked. The term 'erroneous' has not been defined under the Income-tax Act but it is well settled that each and every type of mistake or error committed by the AO cannot be said to be an error. An order can be said to be erroneous if there is incorrect assumption of facts or incorrect application of law in the order by the AO. If the AO after making the enquiries and examining the records taken one of the possible view, it cannot be said that the order passed by the AO was erroneous.

17. We have gone through various case laws as has been cited before us and referred to by my colleagues. In the case of Rampiyari Devi Saraogi Vs CIT 67 ITR 84 (SC), the question involved before the Hon'ble Supreme Court was that no fair and reasonable opportunity was given to the assessee by the Commissioner u/s 33(B) (now Section 263) of the Income Tax Act. In this case the order passed u/s 33(B) of the Act was held to be valid in view of the fact that

there were ample materials to show that the Assessing Officer had made the assessment in undue haste, without any evidence or enquiry.

18. In the case of Tara Devi Agarwal 88 ITR 323 (SC) the assessee had filed voluntary return of the income for assessment year 1955-56 to 1959-60 and the assessment were completed accepting the initial capital and the fact that the assessee was carrying on money lending and speculation business. For the assessment year 1960-61 also voluntary return was filed. The Assessing Officer transferred the case to the other Assessing Officer on the request of the assessee. The Assessing Officer completed the assessment. Subsequently, the CIT reopened the assessment when it was found that the assessment was made on the basis that the income had been earned by the assessee while the assessee was not earning the income and the income would have been assessed in the hands of the other persons at larger amount. It was held that the assessment was erroneous and prejudicial to the interest of the Revenue. The Assessing Officer while remarking that the source of the income of the assessee during the year was income from speculation business and interest on investment stated that neither the assessee was able to produce the details and vouchers of the speculation business made during the year nor there was any evidence regarding the interest received by her from different parties on her investment. Notwithstanding the facts the Assessing Officer did not investigate into the various sources to assess the assessee on a total income of Rs.9,037/-. The action of the CIT u/s 33(B) of the Act is held to be justified canceling the assessment as the Assessing Officer accepted the initial capital, sale of ornament, income from business etc. of the assessee without any enquiry.

19. In the case of CIT Vs Pushpa Devi (supra), Hon'ble Patna High Court also reopened the assessment when the assessment of ladies and minor sons were completed without proper enquiries.

20. In the case of Gee Vee Enterprise 99 ITR 375 (Cal) facts were that the assessee, a private limited company acquired a plot of land and formed a Society for the purpose of making construction. Some of the directors and shareholders with some other registered firm i.e. the assessee. An agreement was entered into between the company and the assessee for making the multi-storied building after taking advances from the licensees to whom flats were to be sold and the agreement came to an end after the building was constructed. The Income Tax Officer granted registration u/s 124 and 185 of the Act and made the assessment accordingly. In the proceedings u/s 263 of the Act assessment was cancelled as the Assessing Officer has not made sufficient enquiries before granting registration and when the matter went before the High Court it was held that it is not necessary for the Commissioner to make further enquiries before canceling the assessment. The Commissioner can record the order as erroneous on the ground that in the facts and circumstances of the case the Assessing Officer ought to have made further enquiries before accepting the statement made by the assessee in the return. The Assessing Officer is not only an adjudicator but also an investigator. He cannot remain passive in the base of a return which is apparent in order but call for further enquiry. It is his duty to ascertain the true facts stated in the return when the circumstances are such as to provoke any enquiry. The word erroneous in Section 263 of the Act includes failure to make such an enquiry. In this case although the assessee had informed to the Assessing Officer that the assessee is a confirming party of the land purchased by the Society but did not enquire under what circumstances the assessee's name appeared as the confirming party, in reality who are the purchasers and to whom

the title of the land passed on at the registration of the documents. The title of the assessee to the project depends on the agreement between the Housing Society and the assessee. Assessee is the confirming party thereto.

21. While in the instant case the proceedings u/s 263 of the Act has been initiated by the CIT not on the basis that the assessee had made entries in the partners' capital account represented by creditors otherwise than credit of money, i.e. transfer of shares held in the name of partners by book entry without the shares having been transferred in the name of the firm. He was of the view that the interest allowed by the AO to the partners on the capital in respect of such credits is not admissible as deduction within the meaning of section 36(1)(iii) read with section 14A. This is a fact that the assessee was not dealing in shares. The dividend income from the shares so transferred to the firm by book entries has been enjoyed by the partners. Even if this income is exempt but it amounts to sharing the profits of the firm otherwise than in accordance with the partnership deed. Ultimately CIT held the assessment order dt. 29.8.03 to be erroneous as well as prejudicial to the interest of the revenue on two grounds one being that the dividends from shares is not appearing in the books of accounts of the assessee and there is no evidence to show that the same is being distributed amongst the partners as per the provisions of the partnership deed and the AO has failed to investigate tbhis issue. Second being the interest against the dividend income is not allowable and the AO has failed to look into this aspect. In my opinion the decision of Hon'ble Supreme court in the case of CIT Vs. Raghunandan Prasad Mody 115 ITR 519 (SC) and that of CIT Vs. Indian Bank Limited 56 ITR 77 (SC) are not applicable to the facts of the case before us. These decision relates to the law as prevailing when Dividend income was not exempt u/s 115O of the Income tax Act and there was no provision prevailing during the impugned assessment as given u/s 14A disallowing the expenditure relating to the

income which do not form part of the total income of the assessee. In my view, the decision of Mrs. Khatiza S. Oomerbhoy vs. ITO (supra) although relied on will support the case of the Revenue, because, in this case, it has been specifically held that if there is non-application of mind on the part of the A.O. or if the A.O. has committed any glaring mistake of fact or law, the order passed will be erroneous and prejudicial to the interest of the Revenue. In that case, I noted that the A.O. has passed an order after examining the accounts, making enquiries and applying his mind and taken one of the views. But, in the case before me, there is no application of mind on the part of the A.O. as the A.O. has not at all made any enquiry or applied his mind on the aspect whether the interest as claimed by the assessee is disallowable in view of the fact that the capital account of the partners have been credited by the shares held in the name of the partners and the dividend income received on the shares was exempt. The assessee has claimed interest on the capital account for which the credit has arisen due to the shares, the income on which is exempt. The provision of section 14A has not at all been examined. This is also fact that the A.O. has also not applied his mind to the fact whether the dividend income as received by the partner on the shares which has been brought into the partnership firm has been brought into the P&L account of the firm or not. This case clearly lays down, if there is lack of enquiry on the part of the A.O., provisions of section 263 of the Act can be applied.

22. The decision of Hon'ble Rajasthan High Court in the case of Bheruram Ratanlal vs. CIT, 257 ITR 795, in my opinion, is not applicable to the facts of the case. This decision relate to the provisions of section 184 as stood prior to these provisions being amended by the Finance Act, 1992 w.e.f. 01.04.1993. In that case, the question relates to the registration of the partnership firm. Now there is no such provision which requires the registration of the partnership firm being granted by the A.O.

23. I have specifically asked the Ld. AR whether there is any evidence on record which may prove that the assessing officer has conducted the enquiry on the points as has been raised by the CIT while issuing notice u/s 263. No enquiry letter or the reply of the assessee being filed during the original assessment proceeding was brought to our knowledge. This clearly prove that in this case, the Assessing Officer failed to carry out the necessary enquiries which he ought to have made before allowing deduction to the assessee u/s 40b in respect of the interest on the capital. I may clarify that section 40b only restricts the claim of the deduction which is otherwise allowable to the assessee under section 37 and section 36(1)(iii) of the Act. Therefore, I am of the view that the other decisions as relied on by the Ld. AR are also not applicable to the facts of this case as those cases also do not relate to the failure on the part of the Assessing Officer to carry out necessary enquiries.

24. I have also gone through the decision of the Hon'ble Supreme Court in the case of CIT Vs Max India Ltd. 295 ITR 282. In this case it was held as under:

> *"The phrase "prejudicial to the interests of the Revenue" in section 263 of the Income-tax Act, 1961, has to be read in conjunction with the expression "erroneous" order passed by the Assessing Officer. Every loss of revenue as a consequence of an order of the Assessing Officer cannot be treated as prejudicial to the interests of the Revenue. For example, when the Assessing Officer adopts one of two courses permissible in law and it has resulted in loss of revenue, or where two views are possible and the Assessing Officer has taken one view with which the Commissioner does not agree, it cannot be treated as an erroneous order prejudicial to the Revenue, unless the view taken by the Assessing Officer is unsustainable in law.*
>
> *Where, on March 5, 1997, at the time when there were prevalent two views of the word "profits" in section 80 HHC, the Commissioner purported to exercise his power under section 263 to revise the order of t he Assessing Officer on the ground that the order passed by the Assessing Officer was prejudicial to the Revenue: Held, that, since section 80 HHC was amended eleven times and different views existed when the Commissioner passed the order and the mechanics of that section had become so complicated over the years, the subsequent amendment of section 80 HHC, even though retrospective, would*

not be attracted. The law as it stood when the Commissioner passed the order dated March 5, 1957, had to be taken into account and the Commissioner had no jurisdiction to interfere in exercise of his powers of revision under section 263."

25. This decision lays down the proposition that the law as it stood when the Commissioner has passed the order has to be taken into account and the subsequent amendment in the Act even though with retrospective effect would not make an order to be erroneous and prejudicial to the interest of the Revenue. Thus, this decision would have assisted the assessee if CIT had invoked the provisions of section 263 of the Act had there been section 14A being inducted subsequently by retrospective amendment. The CIT did not invoke the provisions of section 263 of the Act due to the retrospective amendment but has invoked the provisions of section 263 of the Act due to lack of enquiries being carried out by the Assessing Officer while granting deduction to the assessee u/s 40b) of the Act. I have also gone through the decision of the Hon'ble Supreme Court in the case of Malabar Industrial Co. Vs CIT 243 ITR 83 (SC). In this case it was held as under:-

> *"The pre-requisite to the exercise of jurisdiction by the Commissioner under section 263 is that the order of the AO is erroneous in so far as it is prejudicial to the interests of the revenue. The commissioner has to be satisfied of twin conditions, namely, (i) the order of the assessing officer sought to be revised is erroneous; and (ii) is prejudicial to the interests of the revenue. If one of them is absent- if the order of the Assessing office is erroneous but is not prejudicial to the revenue - recourse cannot be had to section 263(1). There can be no doubt that the provision cannot be invoked to correct each and every type of mistake or error committed by the assessing officer, it is only when an order is erroneous that the section will be attracted. An incorrect assumption of facts or an incorrect application of law will satisfy the requirement of the order being erroneous. <u>In the same category fall orders passed without applying the principles of natural justice or without application of mind</u>. The phrase 'prejudicial to the interest of the revenue' has to be read in conjunction with an erroneous order passed by the assessing officer. Every loss of revenue as a consequence of the order of the assessing officer cannot be treated as prejudicial to the interests of the revenue. For example, if the assessing officer has adopted one of the courses permissible in law and it has resulted in loss of revenue, or where two views are possible and the assessing officer has taken one view with which the commissioner does not agree, it cannot be treated as an*

> *erroneous order prejudicial to the interests of the revenue, unless the view taken by the assessing officer is unsustainable in law. Where a sum not earned by a person is assessed as income in his hands on his so offering the order passed by the assessing officer accepting the same without application of mind as such will be erroneous and prejudicial to the interest of the revenue."*

26. I have also gone through the decision of the Gujarat High Court in the case of CIT Vs Arvind Jewellers 259 ITR 502. In this case the Hon'ble Gujarat High Court has held as under:

> *"Held, that the finding of fact by the Tribunal was that the assessee had produced relevant material and offered explanations in pursuance of the notices issued under section 142(1) as well as section 143(2) of the Act and after considering the material and explanations, the Income-tax Officer had come to a definite conclusion. Since the material was there on record and the said material was considered by the Income-tax Officer and a particular view was taken, the mere fact that different view can be taken should not be the basis for an action under section 263. The order of revision was not justified."*

27. The Hon'ble Gujarat High Court has also followed the decision of the Hon'ble Supreme Court in the case of Malabar Industrial Co. Ltd. Vs CIT 243 ITR 83 (SC). In this case, there is a finding that the assessee has produced relevant materials and offered the explanation and after considering the materials and explanation the Assessing Officer passed the assessment order. This decision, in our opinion will not assist the assessee as in the case of the assessee the Assessing Officer has not carried out necessary enquiry which ought to have been carried out for allowing deduction to the assessee u/s 40b of the Act. Therefore, in my opinion, the order passed by the assessing officer was erroneous and prejudicial to the interest of the Revenue. The CIT has rightly invoked the provisions of section 263 of the Income Tax Act, 1961. I agree with the view taken by the ld. A.M.

28. The matter will now go before the Regular Bench for deciding the appeal in accordance with the majority opinion.

Sd/-
(P.K. BANSAL)
Accountant Member

Place: Agra

Date: 21st January, 2010.

PBN/*

Copy of the order forwarded to:

1. Appellant
2. Respondent
3. CIT concerned
4. CIT (Appeals) concerned
5. DR, ITAT, Agra Bench, Agra
6. Guard File

By Order

Assistant Registrar
Income-tax Appellate Tribunal, Agra

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