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

Date of decision: 12th December, 2012

\+ ITA No.555/2012.

THE COMMISSIONER OF INCOME TAX-V ..... Appellant

Through: Mr. N. P. Sahni, Sr. Standing Counsel with Mr. Ruchesh Sinha, Advocate.

versus

ORIENT CRAFT LTD. ..... Respondents

Through: Mr. Salil Aggarwal with Mr. P. C. Yadav, Advocates

CORAM:
MR. JUSTICE S. RAVINDRA BHAT
MR. JUSTICE R.V. EASWAR

R.V.EASWAR,J: (OPEN COURT)

The substantial question of law proposed by the Revenue in this appeal under Section 260A of the Income Tax Act, 1961 ('Act' for short) is, in short, whether the Income Tax Appellate Tribunal is right in law in holding that the reassessment proceedings under section 147 were not validly initiated.

2. The assessee is a company and for the assessment year 2002-03 it filed a return of income on 31st October, 2002 declaring a total income of Rs.4,45,35,395/-. The return was processed under Section 143(1) on 27th February, 2003; the income returned was accepted. Included in the return was a claim of Rs.8,74,20,642/- under Section 80HHC and Rs.13,35,65,316/- under Section 10B. The assessee was a 100% export-oriented undertaking and was entitled to substantial amounts as duty drawback,

DEPB, premium on DEPB and on sale of quota etc. These were all declared in the profit and loss account and the computation of income.

3. On 15th August, 2005, a notice under Section 148 of the Act was issued reopening the assessment on the ground that income chargeable to tax had escaped assessment. According to the reasons recorded under Section 148(2) for reopening the assessment, the assessee was wrong in treating the proceeds of sale of quota as part of the export turnover for claiming deduction under Section 80HHC. It was also the opinion of the Assessing Officer that the sale proceeds of the quota cannot be considered as export turnover but represented business income covered under Section 28(iv) and had to be reduced to the extent of 90% from the business income as provided by Explanation (baa) to section 80HHC. Not doing so resulted in excessive allowance of the deduction under Section 80HHC and consequently in escapement of income chargeable to tax.

4. In response to the notice under Section 148 the assessee filed a return on 22nd August, 2005 declaring total income at the same figure as in the original return of income; it also questioned the jurisdiction of the Assessing Officer to reopen the assessment and proceed with the reassessment proceedings. In the course of the reassessment proceedings the Assessing Officer dealt with the assessee's objection to the issue of notice under Section 148. He held that the assessee's case was covered by clause(c) of Explanation 2 below Section 147, which provides that claiming excessive deduction would amount to a case of income escaping assessment. He thus rejected the assessee's objection. On merits he held that the assessee was not entitled to any deduction under Section 80HHC in respect of the premium on sale of quota. He also held that the assessee was not entitled to the DEPB of Rs.2,55,74,491/-. The claim under Section 80HHC was thus revised downward to Rs.6,83,94,510/- as against Rs.8,74,20,642/- claimed in the original return which was accepted under Section 143(1). The reassessment order was accordingly passed on 31st October, 2006.

5. Aggrieved, the assessee filed an appeal to the CIT(Appeals) questioning the reassessment order both on the ground of jurisdiction and on merits. The CIT(Appeals) rejected the objection to the jurisdiction and so far as the merits of the assessee's claim are concerned, held that the issue relating to the eligibility of the assessee for the deduction under Section 80HHC in respect of premium on sale of quota was covered in favour of the assessee by the order of the Tribunal in the earlier years as well as the orders passed by his predecessor in the assessee's case for the assessment years 2000-01 and 20001-02 and accordingly upheld the assessee's stand. So far as the deduction claimed under Section 80HHC with reference to the DEPB income is concerned, he held that only the profit on the transfer of DEPB licenses was to be considered for being reduced under Explanation (baa) below Section 80HHC and that 90% of the entire receipts or sale proceeds of the license cannot be reduced from the profits of the business for the purpose of computing the deduction. He accordingly accepted the assessee's working of the deduction with regard to the DEPB income. There were certain other minor issues which were also decided by the CIT(Appeals) who ultimately allowed the assessee's appeal in part.

6. Both the assessee and the Revenue filed appeals to the Income Tax Appellate Tribunal. The assessee challenged the jurisdiction of the Assessing Officer to reopen the assessment under Section 147 as also certain issues on merits which were decided against it by the CIT(Appeals). The Revenue's appeal related to the decision of the CIT(Appeals) in respect of the premium on sale of quota and the DEPB income, both for the purposes of Section 80HHC. The Tribunal took up the appeal of the assessee and examined the reasons recorded for reopening the assessment and held that the only issue on which the assessment was reopened was the deduction under Section 80HHC with reference to premium on sale of export quota which issue had been decided by the Tribunal in the assessee's case for the assessment years 2000-01 and 2001-02 by order dated 7th September, 2005, which orders were followed by the Tribunal for the

assessment years 1999-2000 and 2003-04 vide order dated 21st November, 2008 and that there was no fresh material which came to the notice of the Assessing Officer after the original return was processed under Section 143(1) and having regard to the orders of the Tribunal(supra) and the instruction of the CBDT dated 23rd February, 1998 regarding the treatment to be given to the premium received on transfer of quotas, there was no escapement of income and thus the notice was without jurisdiction. Reference was made to the judgment of the Supreme Court in the case of *CIT vs. Kelvinator of India Ltd.(2010) 320 ITR 561.* Several other authorities were adverted to by the Tribunal and eventually it was observed as under:-

> *"For the above discussion, we hold that since there was no tangible material available with the AO to form the requisite belief of escapement of income, the reopening of the completed assessment is unsustainable in the eye of law. The same is, therefore, cancelled."*

In the above view of the matter, the Tribunal did not examine the merits of the disallowances/additions made in the reassessment order.

7. The Revenue is in appeal before us. The following substantial question of law arises and is framed:-

> *"Was the Tribunal right in law in holding that in the absence of any tangible material available with the Assessing Officer to form the requisite belief regarding escapement of income, the reopening of the assessement made under Section 143(1) is bad in law?"*

8. The Tribunal has extracted the reasons recorded by the Assessing Officer for reopening the assessment. They are as follows:-

> *"On going through the return of income filed by the assessee, it is revealed that while deducting 90% of other income from the profit of business, premium on sale of quota of Rs.17,54,174/- included in the sales was not considered. Therefore omission to deduction 90% of Rs. 17,54,174/- from the profit of business resulted in excess allowance of deduction u/s 80HHC of the Income Tax Act, 1961. In*

> *view of these facts there is reason of believe that the income chargeable to tax has escaped assessment."*

We think that the point taken on behalf of the assessee that even an assessment made under Section 143(1) of the Act can be reopened under Section 147 only subject to fulfillment of the conditions precedent, which include the condition that the Assessing Officer must have "reason to believe" that income chargeable to tax has escaped assessment, is sound. It is true that no assessment order is passed when the return is merely processed under Section 143(1) and an intimation to that effect is sent to the assessee. However, it has been recognised by the Supreme Court itself in *Assistant Commissioner of Income Tax vs. Rajesh Jhaveri Stock Brokers P. Ltd.(2007) 291 ITR 500,* a decision that was relied upon by the revenue, that even where proceedings under Section 147 are sought to be taken with reference to an intimation framed earlier under Section 143(1), the ingredients of Section 147 have to be fulfilled; the ingredient is that there should exist "reason to believe" that income chargeable to tax has escaped assessment. This judgment, contrary to what the Revenue would have us believe, does not give a *carte blanche* to the Assessing Officer to disturb the finality of the intimation under Section 143(1) at his whims and caprice; he must have reason to believe within the meaning of the Section. It would be appropriate to reproduce the following portions from the judgment:-

> *"The scope and effect of section 147 as substituted with effect from April 1, 1989, as also sections 148 to 152 are substantially different from the provisions as they stood prior to such substitution. Under the old provisions of section 147, separate clauses (a) and (b) laid down the circumstances under which income escaping assessment for the past assessment years could be assessed or reassessed. To confer jurisdiction under section 147(a) two conditions were required to be satisfied : firstly the Assessing Officer must have reason to believe that income, profits or gains chargeable to income tax have escaped assessment, and secondly he must also have reason to believe that such escapement has occurred by reason of either omission or failure on the part of the assessee to disclose fully or truly all material facts necessary for his assessment*

of that year. Both these conditions were conditions precedent to be satisfied before the Assessing Officer could have jurisdiction to issue notice under section 148 read with section 147(a). But under the substituted section 147 existence of only the first condition suffices. In other words if the Assessing Officer for whatever reason has reason to believe that income has escaped assessment it confers jurisdiction to reopen the assessment. It is, however, to be noted that both the conditions must be fulfilled if the case falls within the ambit of the proviso to section 147. The case at hand is covered by the main provision and not the proviso.

So long as the ingredients of section 147 are fulfilled, the Assessing Officer is free to initiate proceeding under section 147 and failure to take steps under section 143(3) will not render the Assessing Officer powerless to initiate reassessment proceedings even when intimation under section 143(1) had been issued.

The inevitable conclusion is that the High Court has wrongly applied Adani's case [1999] 240 ITR 224 (Guj) which has no application to the case on the facts in view of the conceptual difference between section 143(1) and section 143(3) of the Act."

We have searched the judgment in vain for the liberty said to have been given to the Assessing Officer by the above judgment that the finality of an intimation under Section 143(1) can be disturbed even by dispensing with the requirement of " reason to believe". On the contrary the observations extracted above reiterate that the intimation can be disturbed by initiating reassessment proceedings only *"so long as the ingredients of Section 147 are fulfilled"* and with reference to Section 143(1) vis-a-vis Section 147, the only ingredient is that there should be reason to believe that income chargeable to tax has escaped assessment and it does not matter that there has been no failure or omission on the part of the assessee to disclose full and true particulars at the time of the original assessment. There is nothing in the language of Section 147 to unshackle the Assessing Officer from the need to show "reason to believe". The fact that the intimation issued under Section 143(1) cannot be equated to an "assessment", a position which has been elaborated by the Supreme Court in the

judgment cited above, cannot in our opinion lead to the conclusion that the requirements of Section 147 can be dispensed with when the finality of an intimation under Section 143(1) is sought to be disturbed. We are at pains to point out this position, which seems fairly obvious to us, because of the argument frequently advanced before us on behalf of the Revenue in other cases as well, under the misconception, if we may say so with respect, that an intimation under Section 143(1) can be disturbed on any ground which appeals to the Assessing Officer. The consequence of countenancing such an argument could be grave. The expression "reason to believe" has come to attain a certain signification and content, nourished over a long period of years by judicial refinement painstakingly embarked upon by great judges in the past. The expression has been judicially interpreted in a particular manner. When Section 147 was recast with effect from 1st April, 1989, the legislature sought to replace the expression "reason to believe" with the expression "for reasons to be recorded by him in writing". But there were representations against the proposal and bowing to them the original expression was restored. This aspect of the matter has been brought out by the Supreme Court in *Commissioner of Income Tax vs. Kelvinator of Income-tax & Anr.(supra)* in the following words:-

> *"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 "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. 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."

9. It would be appropriate at this juncture to take a brief survey of a few decisions of the Supreme Court which have infused meaning and content to the expression "reason to believe" appearing in Section 147.

10. A constitution bench of the Supreme Court in *A.N. Lakshman Shenoy v. ITO (1958) 34 ITR 275*, speaking through S.K. Das, J held that an assessment cannot be reopened on the basis of a mere guess, gossip or rumour. This was in the context of the pre-1948 law relating to reassessment under which the Assessing Officer was empowered to reopen the assessment on the basis of "definite information". Though this judgment is based on the phraseology of Section 34 of the 1922 Act as it existed before 1948 which did not contain the expression "reason to believe", that principle was adopted by the Supreme Court while dealing with Section 34 of the Act after the amendment made in 1948. In that year the words "definite information" were replaced by the words "reason to believe". While expatiating on the new words, a three-Judge Bench of the Supreme Court speaking through V. Ramaswami, J., in *CIT vs S. Narayanappa (1965) 63 ITR 219* opined as under:-

> *"Again the expression "reason to believe" in section 34 of the Income-tax Act does not mean a purely subjective satisfaction on the part of the Income-tax Officer. The belief must be held in good faith: it cannot be merely a pretence. To put it different, it is open to the court to examine the question whether the reasons for the belief have a rational connection or a relevant bearing to the formation of the belief and are not extraneous or irrelevant to the purpose of the section. To this limited extent, the action of the Income-tax Officer in starting proceedings under section 34 of the Act is open to challenge in a court of law (see Calcutta Discount Co. Ltd. v. Income-tax Officer, Companies District 1, Calcutta)."*

In *Sheo Nath Singh vs. Appellate Assistant Commissioner of Income-tax (1971) 82 ITR 147* the Supreme Court (Hegde J) observed as under:-

> *"There can be no manner of doubt that the words " reason to believe " suggest that the belief must be that of an honest and reasonable person based upon reasonable grounds and that the Income-tax Officer may act on direct or circumstances evidence but not on mere suspicion, gossip or rumour. The Income-tax Officer would be acting without jurisdiction if the reason for his belief that the conditions are satisfied does not exist or is not material or relevant to the belief required by the section. The court can always examine this aspect though the declaration or sufficiency of the reasons for the belief cannot be investigated by the court."*

It was further observed that the reasons themselves cannot be stated to be beliefs, which would be an obvious self-contradiction.

11. The entire law as to what would constitute "reason to believe" was summed up by H.R.Khanna, J, speaking for the Supreme Court in Income Tax Officer v Lakhmani Mewaldas (1976) 103 ITR 437. The following principles were laid down:-

(a) The powers of the Assessing Officer to reopen an assessment, though wide, are not plenary.

(b) The words of the statute are "reason to believe" and not "reason to suspect".

(c) The reopening of an assessment after the lapse of many years is a serious matter. Since the finality of a judicial or quasi-judicial proceedings are sought to be disturbed, it is essential that before taking action to reopen the assessment, the requirements of the law should be satisfied.

(d) The reasons to believe must have a material bearing on the question on escapement of income. It does not mean a purely subjective satisfaction of the assessing authority; the reason be held in good faith and cannot merely be a pretence.

(e) The reasons to believe must have a rational connection with or relevant bearing on the formation of the belief. Rational connection postulates that there must be a direct nexus or live link between the material coming to the notice of the Assessing Officer and the formation is belief regarding escapement of income.

(f) The fact that the words "definite information" which were there in section 34 of the Act of 1922 before 1948, are not there in section 147 of the 1961 Act would not lead to the conclusion that action can now be taken for reopening an assessment even if the information is wholly vague, indefinite, far-fetched or remote.

12. In *Commissioner of Income Tax vs. Kelvinator of Income-tax & Anr.* (supra) the Supreme Court observed as under:-

> *"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 "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."*

It was also observed that after 1.4.1989 the Assessing Officer has power to reopen provided there is "tangible material" to come to the conclusion that there is escapement of income. This judgment has laid emphasis on two more aspects: that there can be no review of an assessment in the guise of reopening and that a bare review without any tangible material would amount to abuse of the power.

13. Having regard to the judicial interpretation placed upon the expression "reason to believe", and the continued use of that expression right from 1948 till date, we have to understand the meaning of the expression in exactly the same manner in which it has been understood by the courts. The assumption of the Revenue that somehow the words "reason to believe" have to be understood in a liberal manner where the finality of an intimation under Section 143(1) is sought to be disturbed is erroneous and misconceived. As pointed out earlier, there is no warrant for such an assumption because of the language employed in Section 147; it makes no distinction between an order passed under section 143(3) and the intimation issued under section 143(1). Therefore it is not permissible to adopt different standards while interpreting the words "reason to believe" vis-à-vis Section 143(1) and Section 143(3). We are unable to appreciate what permits the Revenue to assume that somehow the same rigorous standards which are applicable in the interpretation of the expression when it is applied to the reopening of an assessment earlier made under Section 143(3) cannot apply where only an intimation was issued earlier under Section 143(1). It would in

effect place an assessee in whose case the return was processed under Section 143(1) in a more vulnerable position than an assessee in whose case there was a full-fledged scrutiny assessment made under Section 143(3). Whether the return is put to scrutiny or is accepted without demur is not a matter which is within the control of assessee; he has no choice in the matter. The other consequence, which is somewhat graver, would be that the entire rigorous procedure involved in reopening an assessment and the burden of proving valid reasons to believe could be circumvented by first accepting the return under Section 143(1) and thereafter issue notices to reopen the assessment. An interpretation which makes a distinction between the meaning and content of the expression "reason to believe" in cases where assessments were framed earlier under Section 143(3) and cases where mere intimations were issued earlier under Section 143(1) may well lead to such an unintended mischief. It would be discriminatory too. An interpretation that leads to absurd results or mischief is to be eschewed.

14. Certain observations made in the decision of *Rajesh Jhaveri (supra)* are sought to be relied upon by the revenue to point out the difference between an "assessment" and an "intimation". The context in which those observations were made has to be kept in mind. They were made to point out that where an "intimation" is issued under section 143(1) there is no opportunity to the assessing authority to form an opinion and therefore when its finality is sought to be disturbed by issuing a notice under section 148, the proceedings cannot be challenged on the ground of "change of opinion". It was not opined by the Supreme Court that the strict requirements of section 147 can be compromised. On the contrary, from the observations (quoted by us earlier) it would appear clear that the court reiterated that *"so long as the ingredients of section 147 are fulfilled"* an intimation issued under section 143(1) can be subjected to proceedings for reopening. The court also emphasised that the only requirement for disturbing the finality of an intimation is that the assessing officer should have "reason to believe" that income chargeable to tax has escaped assessment. In our opinion, the

said expression should apply to an intimation in the same manner and subject to the same interpretation as it would have applied to an assessment made under section 143(3). The argument of the revenue that an intimation cannot be equated to an assessment, relying upon certain observations of the Supreme Court in *Rajesh Jhaveri (supra)* would also appear to be self-defeating, because if an "intimation" is not an "assessment" then it can never be subjected to section 147 proceedings, for, that section covers only an "assessment" and we wonder if the revenue would be prepared to concede that position. It is nobody's case that an "intimation" cannot be subjected to section 147 proceedings; all that is contended by the assessee, and quite rightly, is that if the revenue wants to invoke section 147 it should play by the rules of that section and cannot bog down. In other words, the expression "reason to believe" cannot have two different standards or sets of meaning, one applicable where the assessment was earlier made under section 143(3) and another applicable where an intimation was earlier issued under section 143(1). It follows that it is open to the assessee to contend that notwithstanding that the argument of "change of opinion" is not available to him, it would still be open to him to contest the reopening on the ground that there was either no reason to believe or that the alleged reason to believe is not relevant for the formation of the belief that income chargeable to tax has escaped assessment. In doing so, it is further open to the assessee to challenge the reasons recorded under section 148(2) on the ground that they do not meet the standards set in the various judicial pronouncements.

14. In the present case the reasons disclose that the Assessing Officer reached the belief that there was escapement of income *"on going through the return of income"* filed by the assessee after he accepted the return under Section 143(1) without scrutiny, and nothing more. This is nothing but a review of the earlier proceedings and an abuse of power by the Assessing Officer, both strongly deprecated by the Supreme Court in *CIT vs. Kelvinator (supra)*. The reasons recorded by the Assessing

Officer in the present case do confirm our apprehension about the harm that a less strict interpretation of the words "reason to believe" vis-à-vis an intimation issued under section 143(1) can cause to the tax regime. There is no whisper in the reasons recorded, of any tangible material which came to the possession of the assessing officer subsequent to the issue of the intimation. It reflects an arbitrary exercise of the power conferred under section 147.

15. For the above reasons, we answer the substantial question of law framed by us in the affirmative, in favour of the assessee and against the Revenue. The appeal of the Revenue is accordingly dismissed. There shall be no order as to costs.

R.V.EASWAR, J

S. RAVINDRA BHAT, J

December 12, 2012
Bisht