

Indian Aluminium Co. Ltd. Vs Deputy Commissioner of Income Tax and Others

Court: Calcutta High Court

Date of Decision: Aug. 3, 2010

Acts Referred: Income Tax Act, 1961 & Section 141(A), 142, 142(2)(A), 158(B)(E), 288(2)

Citation: (2010) 329 ITR 550

Hon'ble Judges: Aniruddha Bose, J

Bench: Single Bench

Advocate: Debiprosad Pal, Abhratosh Majumder, M. Seal and Nilanjana Pal Banerjea, for the Appellant; Deepak K. Shome and S.B. Saraf, for the Respondent

Final Decision: Allowed

Judgement

Aniruddha Bose, J.

The Petitioner before me is an existing public company within the meaning of the Companies Act, 1956. In this writ

petition, the Petitioner has challenged an order issued u/s 142(2A) of the Income Tax Act, 1961 directing audit of their accounts by an accountant

nominated by the Chief Commissioner of Income Tax, Calcutta-3 (CCIT) in respect of the assessment year 1987-88. The order was passed on

June 12, 2007, a copy of which has been made annexure P9 to the writ petition.

2. The dispute which led to passing of the impugned order originated in the year 1989 when the Petitioner was directed through its principal officer

to furnish certain informations specified in a notice issued on December 29, 1989, in respect of the said assessment year. For the subject

assessment year, the Petitioner had filed their return declaring loss of Rs. 5,48,58,580, along with audited annual report, as well as tax audit report.

It is pleaded in the petition that provisional assessment in respect of the Petitioner's return was made u/s 141A of the Act and the Assessing

Officer had directed refund of a sum of Rs. 1,42,22,980. The Petitioner claims to have furnished their response to the notice dated December 29,

1989 but it appears that the authorities were not satisfied with such response. On August 27, 1990 another notice was issued detailing the

particulars on which the Income Tax authorities wanted further information/clarification. Correspondence was being exchanged between the

Petitioner and the Income Tax authorities in this regard but the Income Tax authorities were still not satisfied with the response of the Petitioner.

Eventually by a communication issued on February 27, 1991, the Petitioner was informed that audit had been proposed in the case of the

Petitioner in accordance with the provisions of Section 142(2A) of the Act, and Shri P. ML Narielwala, chartered accountant of M/s. S.R.

Batliboi and Co. was being appointed as the nominated accountant under the said provisions of the Act. This order was challenged by the

Petitioner before this Court by filing a writ petition, which was registered as Matter No. 1019 of 1991. This writ petition was eventually allowed by

the hon"ble single judge of this Court on January 5, 2007. His Lordship held:

Subject-matter of challenge in this writ petition is an order dated February 27, 1991, passed u/s 142(2A) of the Income Tax Act appointing a

special auditor. Dr. Pal, learned senior advocate appearing for the writ Petitioner submitted that the order was passed without complying with the

principles of natural justice, that is to say without giving opportunity of hearing to the writ Petitioner and the same is patently bad. In support of his

submission he relied on a judgment of the apex court in the case of Rajesh Kumar and Others Vs. D.Commissioner of Income Tax and Others, .

Md. Nizamuddin, learned Counsel appearing for the Department took time to consider the matter. After considering the matter he very fairly

submitted that in view of the judgment cited by Dr. Pal he really cannot contest the point that a show-cause notice should have been given before

passing an order u/s 142 of the Income Tax Act.

Considering the submission made by the learned advocates for the parties the order dated February 27, 1991 is set aside.

It will be open to the Department to take further steps in accordance with law.

An urgent certified copy of this order be made available to the parties, if applied for upon compliance with all requisite formalities.

3. After this judgment was delivered, a fresh notice under Sub-section (1) of Section 142 of the Act was issued on January 11, 2007 stipulating:

Sir/Madam,

In connection with the assessment for the assessment year 1987-88 you are required to:

(a) . . .

(b) . . .

(c) furnish in writing and verified in the prescribed manner information called for as per the enclosed letter of even date and on the points or matters

specified therein before me at my office at Aayakar Bhawan, 5th Floor, P-7 Chowringhee Square, Kolkata-69 on January 15, 2007 at 2.

4. This communication was issued by the Deputy Commissioner of Income Tax of the relevant circle.

5. It appears that the matter was attended to on January 17, 2007, instead of January 15, 2007, as submitted on behalf of the Petitioner. The

contention of the Respondent authorities, however, is that none had appeared on behalf of the Petitioner on that date. Another notice under the

same provision was issued on April 19, 2007, requiring the Petitioner to disclose certain information in the prescribed manner. This letter stipulates:

Sir/Madam,

In connection with the assessment for the assessment year 1987-88 you are required to:

(a) . . .

(b) . . .

(c) furnish in writing and verified in the prescribed manner information called for as per the enclosed letter of even date and on the points or matters

specified therein before me at my office at Aayakar Bhawan, 5th Floor, P-7 Chowringhee Square, Kolkata-69 on April 25, 2007 at 1.30 p.m.

6. The case of the Petitioner is that no enclosure was given to the said letters but the representative of the Petitioner had attended the hearing on

the respective dates and filed all the details before Respondent No. 1 in the form of a paper book. This again has been disputed by the learned

Counsel for the Income Tax authorities in course of hearing. Thereafter, the Deputy Commissioner of Income Tax, Headquarters-III, Kolkata,

informed the Petitioner in writing on behalf of the Chief Commissioner of Income Tax, Calcutta 3, that proposal had been received by the Chief

Commissioner of Income Tax for special audit under the provisions of Section 142(2A) of the Act in respect of the subject assessment year. This

communication dated 4 June 2007 provides:

Sub: Special audit u/s 142(2A) of the Income Tax Act, 1961, for the assessment year 1987-88--Matter regarding.

Apropos of the above subject, I have been directed to inform you that proposal has been received by the Chief Commissioner of Income Tax,

Kolkata-III form the field formation for a special audit u/s 142(2A) for the aforesaid assessment year.

During the course of assessment proceedings it has been observed that the company, manufacturer of aluminium products, had several units spread

all over the country. The transactions were huge in nature and details were voluminous. In spite of giving reasonable opportunities of being heard,

all the details in the manner called for were not filed. Considering the magnitude of the expenditure and inadequate details available in the accounts

submitted, it is extremely difficult to examine the veracity as well as allowability of the claimed expenses to determine the total income of the

company.

In view of the above reasons, considering the aforesaid nature and complexity of the accounts, your case is being considered for invoking the

provisions u/s 142(2A) of the Income Tax Act for special audit.

I have been directed to request you to appear before the Chief Commissioner of Income Tax, Kol-III, Kol at 12.30 p.m. on June 7, 2007 in his

chamber (R. No. 2/31) in the 2nd floor of Aayakar Bhavan for the hearing on the subject.

7. On June 7, 2007, however, the Petitioner had sought adjournment and the matter was heard on June 11, 2007, before the Chief Commissioner

of Income Tax. The Petitioner had also responded in writing on June 11, 2007, to the said proposal indicating that there was no necessity of

appointment of special auditor and outlined their reason on the basis of which the proposal for special audit was being resisted by them. On June

12, 2007, an order was passed by the Chief Commissioner of Income Tax nominating Sri Somnath Bhattacharya, to act as accountant within the

meaning of Section 142(2A) of the Act for audit of the accounts of the Petitioner in respect of the subject financial year. The Assessing Officer,

being the Deputy Commissioner of Income Tax had passed the order directing special audit on the following grounds:

The Assessee-company, M/s. Indian Aluminium Co. Ltd. is engaged in the business of manufacturing aluminium products. The Assessee has units

at various places in the country. In the revised return of income filed on March 7, 1999, the Assessee-company claimed loss of Rs. 5,94,83,914.

The Assessee has claimed total expenditure, i.e., Rs. 23,731.41 lakhs broadly under four head. The main item of expenditure, i.e., Rs. 17,815.71

lakhs has been shown in the head of "cost of sales". Further, substantial expenditure has been claimed under sub-heads like "power and fuel" (Rs.

5,605.50 lakhs) and "salary, wages and bonus" (Rs. 2,028.33 lakhs). In addition, the expenses under sub-head "other expenditure" are at Rs.

413.89 lakhs. The case was selected for scrutiny and the Assessing Officer requested the Assessee to submit certain details in order to examine

the claims of the Assessee.

The Assessee has filed details from time to time but these submissions are mostly in the nature of unit-wise numerical break-up of the expenses and

the detailed evidences including bills and vouchers in respect of all items were not produced before the Assessing Officer. The operations of the

Assessee company are huge and there is sufficient complexity involved. Considering the magnitude of expenditure and inadequate details available

in the accounts submitted, it is extremely difficult to examine the genuineness as well as allowability of the claimed expenses in order to determine

the total income of the Assessee.

In view of the above, the Assessee-company is directed to get its accounts audited u/s 142(2A) in respect of issues enumerated below by Shri

Somnath Bhattacharya of P-20, Durga Charan Mitra Street, Kolkata-700 006, the auditor nominated for this purpose by the Chief Commissioner

of Income Tax, Kolkata-III, Kolkata vide his order No. CC- III/142(2A)/2007-08/98, dated June 12, 2007. The auditor shall furnish the report

in the prescribed format within 60 days of receipt of this order.

8. The said order also specified the scope of the audit, stipulating the subject-heads in respect of which the audit was to be conducted. These

include public deposits, item/unit-wise accounts, cost of imported assets and investment allowance thereon, research and development and

scientific research expenses, etc.

9. This order, as also the order of the Chief Commissioner of Income Tax are under challenge in this writ petition and the main ground of challenge

is violation of the principles of natural justice on the part of the Income Tax authorities while issuing the impugned order. It has been contended on

behalf of the Petitioner that they did not have proper opportunity to explain their case before the Income Tax authorities in justification of their

stand that no such audit was warranted. Three decisions have been primarily relied on by Dr. Pal, learned senior counsel appearing for the

Petitioner in support of his submissions. These are two judgments of the hon"ble Supreme Court in the cases of (i) being Rajesh Kumar and Others

Vs. D.Commissioner of Income Tax and Others, (ii) Sahara India (Firm), Lucknow Vs. Commissioner of Income Tax, Central-I and Another, and

a decision of the hon"ble single judge of this Court in the case of West Bengal State Co-operative Bank Ltd. Vs. Joint Commissioner of Income

Tax and Others, It has also been argued by Dr. Pal that in the present case, the factual position did not justify invocation of power under the

provisions of Section 142(2A). He submitted that there was no complexity of the accounts involved in the case of the Petitioner in respect of the

subject assessment year.

10. Complaint has been made on behalf of the Petitioner that the letter dated January 11, 2007, did not contain any enclosure. A letter, however,

addressed to the Petitioner containing the points on which information was sought has been annexed to the affidavit-in-opposition marked ""C"" ,

originating from the office of the Deputy Commissioner of Income Tax, Special Range-13. In this letter, the Petitioner has been asked to disclose

informations against thirty-three subject heads. The case of the Income Tax authorities is that such requisition was sent to the Petitioner along with

the notice dated December 29, 1989, but the Petitioner did not respond to such requisition.

11. Further case of the Petitioner is that the notice issued by the Income Tax authorities on April 19, 2007, which required the Petitioner to

disclose information/particulars on April 25, 2007, did not specify that the said date was fixed for hearing on the aspect of appointment of a

chartered accountant in terms of Section 142(2A) of the Act. It has been urged that at the time of hearing on that date, i.e., April 25, 2007, the

Assessing Officer did not intimate the Assessee that hearing was posted the proposal for appointment of a chartered accountant for special audit.

12. On this count, it has been argued that the Assessing Officer did not give opportunity of hearing to the Petitioner before sending the proposal.

As regards hearing before the Chief Commissioner of Income Tax, the case of the Petitioner is that the documents based on which the Chief

Commissioner had passed the order were never made available to the Petitioner. The Petitioner's specific grievance is that the report of the

Assessing Officer on the basis of which the Chief Commissioner of Income Tax passed the order was never furnished to the Petitioner. The said

report was disclosed for the first time in the order of approval dated June 12, 2007, and the proposal for approval was also not supplied to the

Petitioner. It is also the case of the Petitioner that in terms with the proviso to Section 142(2A) of the Income Tax Act, no opportunity of being

heard had been afforded to the Petitioner before the order u/s 142(2A) was passed on 12 June after obtaining the approval of the Chief

Commissioner of Income Tax.

13. When the judgment of the Supreme Court was delivered in the case of Rajesh Kumar and Others Vs. D. Commissioner of Income Tax and

Others, there was no specific provision in the statute requiring the Income Tax authorities to provide opportunity of hearing to an Assessee before

passing an order under the provisions of Section 142(2A) of the Act. Subsequent to the passing of the said order, a proviso to Section 142(2A)

was introduced by way of an amendment and the said provision subsequent to the amendment provides:

(2A) If, at any stage of the proceedings before him, the Assessing Officer, having regard to the nature and complexity of the accounts of the

Assessee and the interests of the Revenue, is of the opinion that it is necessary so to do, he may, with the previous approval of the Chief

Commissioner or Commissioner direct the Assessee to get the accounts audited by an accountant, as defined in the Explanation below Sub-section

(2) of Section 288, nominated by the Chief Commissioner or Commissioner in this behalf and to furnish a report of such audit in the prescribed

form duly signed and verified by such accountant and setting forth such particulars as may be prescribed and such other particulars as the

Assessing Officer may require:

Provided that the Assessing Officer shall not direct the Assessee to get the accounts so audited unless the Assessee has been given a reasonable

opportunity of being heard.

14. The hon"ble Supreme Court in the case of Rajesh Kumar and Others Vs. D.Commissioner of Income Tax and Others, held that without giving

an opportunity of hearing, such order could not be passed. Another Bench of the court of the hon"ble Supreme Court took a different view. The

matter was thereafter referred to a three-judge Bench of the hon"ble Supreme Court. The Bench comprising of three hon"ble judges of the

Supreme Court in the decision of Sahara India (Firm), Lucknow Vs. Commissioner of Income Tax, Central-I and Another, sustained the view

taken by the in the case of Rajesh Kumar and Others Vs. D.Commissioner of Income Tax and Others, . The other amendment which was

introduced to the aforesaid provision was that the fees of the statutory auditor was to be paid by the income tax authorities. The said provision, as

it originally stood, required the Assessee to pay the fees of the statutory auditor.

15. It was sought to be argued on behalf of the Income Tax authorities that since there was no obligation on the part of the Assessee to pay the

fees for audit anymore, the requirement for compliance with the principles of natural justice was no more necessary as a direction for special audit

did not have any adverse civil consequence. But, in my opinion, merely because fees are no more required to be paid by the Assessee, the

operation of an order under the aforesaid provision does not become immune from a challenge on the ground of breaching the principles of natural

justice. I am unable to accept this submission. This question was examined by the hon"ble Supreme Court in the case of Sahara India (Firm),

Lucknow Vs. Commissioner of Income Tax, Central-I and Another, , and it was held (page 417):

In the light of the aforesaid legal position, we are in respectful agreement with the decision of this Court in Rajesh Kumar that an order u/s

142(2A) does entail civil consequences. At this juncture, it would be relevant to take note of the insertion of the proviso to Section 142(2D) with

effect from June 1, 2007. The proviso provides that the expenses of the auditor appointed in terms of the said provision shall, henceforth, be paid

by the Central Government. In view of the said amendment, it can be argued that the main plank of the judgment in Rajesh Kumar to the effect that

direction u/s 142(2A) entails civil consequences because the Assessee has to pay substantial fee to the special auditor is knocked off. True it is that

the payment of auditor's fee is a major civil consequence, but it cannot be said to be the sole civil or evil consequence flowing from directions u/s

142(2A). We are convinced that special audit has an altogether different connotation and implications from the audit u/s 44AB. Unlike the

compulsory audit u/s 44AB, it is not limited to mere production of the books and vouchers before an auditor and verification thereof. It would

involve submission of explanation and clarification which may be required by the special auditor on various issues with relevant data, document,

etc., which in the normal course, an Assessee is required to explain before the Assessing Officer. Therefore, special audit is more or less in the

nature of an investigation and in some cases may even turn out to be stigmatising.

16. Now, that the necessity for complying with the principles of natural justice on the part of the Income Tax authorities stands established even

after the amendment of the aforesaid provision, I shall examine the question as to whether there has been actual violation of the principles of natural

justice in this case.

17. Mr. Shome, learned senior advocate appearing for the Income Tax authorities has submitted that in the present case notices were issued and

the Petitioner was actually heard. He refers to the notices dated 11 January 2007 and 20 April 2007 and refers to the order sheet recording the

proceeding of 25 April 2007. He further submits that before approving the proposal, the Chief Commissioner of Income Tax had also given

opportunity of hearing to the Petitioner. The Income Tax authorities have also disputed allegation that any paper book containing the documents

had been filed. In any event it is their case that the reply to the queries was required to be filed as per format. This was admittedly not done.

18. On the argument that the proposal was not made available to the Petitioner and the reason for sending the proposal was not communicated to

them, the stand of the Income Tax authorities is that the reason for which such audit was proposed was communicated to the Petitioner's

representative and that the matter was discussed with them.

19. From the records, I find that the two notices dated January 11, 2007 and April 19, 2007, required the Petitioner to disclose the informations

called for as per the letter enclosed thereto. It was further stipulated that the reply was to be furnished at the Office of the Deputy Commissioner

on the stipulated dates at 1.30 p.m. Neither of these two notices specified that the said date was being fixed for hearing of the Petitioner as regards

proposal for audit in terms of Section 142(2A) of the Act. The minutes of the proceeding before the Income Tax authorities on 25 April 2007 has

been annexed at page 25 of the affidavit-in-opposition filed on behalf of the Income Tax authorities. This provides:

Sri A.C. Banerjee and Sri R. Sinharay, authorised representatives of the Assessee of the company appeared for the case. The authorised

representative stated that the Assessee has given from its side all the replies to the questions as per requisition dated December 29, 1989 and no

new/further details are to be submitted now from the side of the Assessee. The case was heard and discussed.

20. From such recordal, it appears that the proceeding was confined to the aspects of furnishing all details but no effective hearing took place.

What is recorded is that the case was heard and discussed. Admittedly, the proposal was not given to the Petitioner before hearing took place

before the Chief Commissioner of Income Tax.

21. For conducting the process of approval the Supreme Court has laid down a strict guideline in the case of Rajesh Kumar and Others Vs.

D. Commissioner of Income Tax and Others, it has been held, in the facts of that case (page 110 and 111):

In this case itself the Appellants were not made known as to what led the Deputy Commissioner to form an opinion that all relevant factors

including the ones mentioned in Section 142(2A) of the Act are satisfied. If even one of them was not satisfied, no order could be passed. If the

attention of the Commissioner could be drawn to the fact that the underlying purpose for appointment of the special auditor is not bona fide he

might not have approved the same.

Assuming that two sets of accounts were being maintained the same would not mean that the nature of accounts is difficult to understand. It could

have furthermore not been shown that the power is sought to be exercised only for an unauthorised purpose, viz., for the purpose of extension of

the period of limitation as provided for under Explanation 2 to Section 158BE of the Act.

An order of approval is also not to be mechanically granted. The same should be done having regard to the materials on record. The explanation

given by the Assessee, if any, would be a relevant factor. The approving authority was required to go through it. He could have arrived at a

different opinion. He in a situation of this nature could have corrected the Assessing Officer if he was found to have adopted a wrong approach or

posed a wrong question unto himself. He could have been asked to complete the process of assessment within the specified time so as to save the

Revenue from suffering any loss. The same purpose might have been achieved upon production of some materials for understanding the books of

account and/or the entries made therein. While exercising his power, the Assessing Officer has to form an opinion. It is final so far as he is

concerned albeit subject to approval of the Chief Commissioner or the Commissioner, as the case may be. It is only at that stage he is required to

consider the matter and not at a subsequent stage, viz., after the approval is given.

22. In the facts of the present case also, I do not find any material from where it can be inferred that it was made known to the Petitioner as to

what led the Deputy Commissioner to form an opinion that all relevant factors including the ones mentioned in Section 142(2A) stood satisfied. In

the absence of these materials being made available, it would not have been possible for the Petitioner to effectively deal with the proposal or draw

attention of the Chief Commissioner of Income Tax that the purpose for directing the special audit was unwarranted or not bona fide. In the

affidavit-in-opposition, it has been stated that the reasons as to why the proposal was sent was discussed before the Chief Commissioner of

Income Tax. But I do not think making materials available at the time of hearing would constitute affording sufficient opportunity to defend the

Petitioner's stand before the Chief Commissioner of Income Tax against granting of approval to the proposal for special audit. It is also a facet of

natural justice that a person should have access to materials which could be used against him by an authority to enable such person to effectively

utilise the opportunity of hearing. Unless an Assessee has the access to the materials on the basis of which the Chief Commissioner of Income Tax

would consider the question of granting approval to special audit, such opportunity of hearing would degenerate into an idle formality. The

Assessee must have knowledge before participating in hearing before the Chief Commissioner of Income Tax at the approval stage the basis of the

proposal for special audit. The factors on the basis of which the question of granting approval to a proposal for special audit is examined, are all

complex factors, as complexity is the key reason for directing special audit. In the event the report of the Assessing Officer to which reference has

been made by the Chief Commissioner of Income Tax in the order of approval and the proposal are made available to the Assessee only at the

stage of hearing on the question of granting approval, that would not constitute sufficient opportunity so far as the Assessee would be concerned,

to enable them to effectively resist grant of approval. Under these circumstances, in my opinion, the principles of natural justice were breached, as

the Petitioner was not given sufficient opportunity to present their case at the approval stage before the Chief Commissioner of Income Tax.

23. Arguments were also advanced before me that there was no complexity of the accounts involved in the present case that would have

warranted initiation of proceeding u/s 142(2A) of the Act. Several authorities were cited by the learned Counsel appearing for the respective

parties on that point. Mr. Shome referred to the decisions of the hon"ble Supreme Court in the case of Living Media Ltd. Vs. Commissioner of

Income Tax and Another, a decision of a Division Bench of this Court in the case of Joint Joint Commissioner of Income Tax Vs. I.T.C. Ltd. and

Another, and a Bench decision of the hon"ble Delhi High Court in the case of Gurunank Enterprises and Bhagya Rekha Enterprises Vs. The

Commissioner of Income Tax and Another, . I am of the opinion that since I am satisfied that the principles of natural justice stood breached in the

case of the Petitioner, the point as to whether the facts of this case or the nature of accounts justified as special audit ought to be re-examined by

the Chief Commissioner of Income Tax upon giving the Petitioner a fresh hearing. I do not think it is necessary to deal with the decision of the

Calcutta High Court reported in West Bengal State Co-operative Bank Ltd. Vs. Joint Commissioner of Income Tax and Others, on its own, as

this is also an authority for the proposition that opportunity of hearing is necessary before an order under the said provision can be issued. The two

authorities of the Supreme Court of India cover this issue and approve this view.

24. Under these circumstances, I quash the impugned order of approval, nomination of the accountant and direction for special audit. Let the Chief

Commissioner of Income Tax re-examine the proposal for grant of approval upon giving the Petitioner an opportunity of hearing. At least three

weeks before such hearing is fixed, the Petitioner shall be made available the materials which originated from office of the Assessing Officer on the

basis of which approval of the Chief Commissioner of Income Tax is sought, if such materials have already not been disclosed to the Petitioner.

This would include the proposal for special audit and the report of the Assessing Officer, if any. The writ petition stands allowed in the above

terms.

25. There shall, however, be no order as to costs.

Later:

26. Urgent photostat certified copy of this judgment be given to the learned advocates for the parties, if applied for, as expeditiously as possible.