Purity Techtextile (P) Ltd. Vs Assistant Commissioner of Income Tax and Another

Court: Bombay High Court

Date of Decision: Feb. 8, 2010

Acts Referred: Constitution of India, 1950 â€" Article 226
Income Tax Act, 1961 â€" Section 143(1), 143(3), 147, 148, 149
State Financial Corporations Act, 1951 â€" Section 29

Citation: (2010) 230 CTR 157 : (2010) 325 ITR 459 : (2010) 189 TAXMAN 21

Hon'ble Judges: J.P. Devadhar, J; D.Y. Chandrachud, J

Bench: Division Bench

Advocate: S.E. Dastoor, Nishant Thakkar and Rajesh Poojari, instructed, Mint and Confreres, for the Appellant; J.S. Saluja, for the Respondent

Judgement

D.Y. Chandrachud, J.
Rule, returnable forthwith. By consent of the learned Counsel for the parties, the petition is taken up for hearing and

final disposal.

2. The challenge in these proceedings under Article 226 of the Constitution of India is to the reopening of assessments for asst. yrs. 2003-04 and

2004-05 by notices dt. 24th March, 2009 and 31st March, 2009 in purported exercise of powers u/s 148 of the IT Act, 1961.

3. The assessee claimed a deduction u/s 80IB of the Act commencing from asst. yr. 2001-02. The assessee claims to have set up an industrial

undertaking in an industrially backward area at Nani Daman. Briefly stated, from the record of the Court it appears that the Maharashtra State

Financial Corporation ("MSFC") had granted loan facilities to a company by the name of Innovative Plastics (P) Ltd. The company was in default

of the payment of its dues, following which MSFC exercised its powers u/s 29 of the State Financial Corporations Act and sold the land and

building to Khosla Filters (P) Ltd. under a deed of conveyance dt. 24th Dec, 1999 for consideration. The purchaser granted a lease of the

property on 29th Dec, 1999 to the petitioner for a period of ten years. The petitioner sought registration as a small scale unit for manufacturing

filter bags, filter panels, made ups of cotton and manmade fabrics. Provisional registration was granted to the petitioner by the Director of

Industries on 3rd March, 2000. The petitioner made an investment of Rs. 7,19,447 for the purchase of plant and machinery and set up an

industrial undertaking on the property. Industrial production commenced from 6th April, 2000 and a permanent license was received on 19th Feb.,

2001.

4. The petitioner made its claim for the first time in respect of the profits derived from the industrial undertaking u/s 80IB of the Act for asst. yr.

2001-02. The case of the petitioner for asst. yr. 2001-02 was selected for scrutiny and during the course of the assessment proceedings, queries

were raised with respect to the entitlement of the petitioner to claim a deduction u/s 80IB. By its letter dt. 3rd Dec, 2002, the petitioner submitted

details as regards the setting up of the industrial undertaking. An order of assessment was passed u/s 143(3) of the Act on 31st Oct., 2002 for

asst. yr. 2001-02. A deduction u/s 80IB was allowed. The return for asst. yr. 2002-03 claiming a deduction u/s 80IB was processed u/s 143(1)

(a). For asst. yr. 2002-03, an order of assessment was passed u/s 143(3). During the course of the assessment proceedings, the petitioner inter

alia submitted its certificate of registration as an SSI unit and an audit report in Form 10CCB. Among the details disclosed included the

circumstance that a license to work had been issued by the local authority. A copy of the license to work the factory issued on 14th Aug., 2000 by

the Chief Inspector of factories, Daman was annexed to the Form 10CCB. The license contains a specific endorsement to the effect that the plans

had been approved by the Sarpanch on 12th Sept., 1988. Further details were filed by the petitioner by a letter dt. 25th Jan., 2005 during the

course of assessment proceedings for asst. yr. 2003-2004, including the certificate of registration as an SSI unit and the power connection release

order. On 28th Feb., 2005, an assessment order was passed u/s 143(3) of the Act for asst. yr. 2003-04. The assessment order duly notes that the

assessee had claimed a deduction u/s 80IB of the Act for the unit which was set up in an industrially backward area and that Form 10CCB was

available on record.

5. The petitioner was allowed the benefit of a deduction u/s 80IB of the Act for asst. yrs. 2004-05, 2005-06 and 2006-07. On 24th March, 2009

and 31st March, 2009 the assessment for asst. yrs. 2003-04 and 2004-05 was sought to be reopened in exercise of powers u/s 148 of the Act.

The reasons which have been recorded by the AO note that the assessee had taken an industrial unit at Daman on rent from an associate concern

and that a deduction had been allowed u/s 80IB for asst. yrs. 2003-04 and 2004-05. However during the course of the assessment proceedings

for a subsequent year, it was observed that the factory had been purchased by Khosla Investment (P) Ltd. and was given on license to the

assessee. The notices record that the plan of the factory premises was approved by the Sarpanch on 12th Sept., 1988, which would show that the

industrial unit was already in existence and in the use of some other person for the purpose of availing benefits provided under the Act. In the case

of the assessee, it has been stated that the factory plan having been approved twelve years prior to the commencement of the business of the

assessee, that would lead to an inference that the business/industrial unit of the assessee had come into existence at the place where the business of

someone else was already in existence and that the other party had availed of the benefit provided in the Act. A reference has been made to the

provisions of Section 80IB of the Act to suggest that one of the conditions for claiming a deduction is that the business should not be formed either

by splitting up or by reconstruction of a business already in existence.

6. The assessee filed objections to the reasons recorded by the AO. While disputing that there was reason to believe that income had escaped

assessment within the meaning of Section 147, the assessee submitted that : (i) The sale by MSFC was only of the land and building and that it was

the assessee which had installed the plant and machinery; (ii) There was absolutely no basis in the statement of the Revenue that the business of the

assessee had been formed by splitting up or reconstruction of a business already in existence; and (iii) The reassessment notice appeared to have

been issued pursuant to an audit report and the AO had no reason to believe that income had escaped assessment.

7. The objections were dealt with by the AO and disposed of by an order dt. 13th Nov., 2009. The AO has once again reiterated that during the

course of subsequent proceedings, a copy of the license was filed by the assessee, which states that the plan for the factory was approved by the

Sarpanch on 12th Sept., 1988. According to the AO, this document was not produced or submitted by the assessee during the course of the

assessment proceedings for earlier years. Consequently, according to the AO, there was valid reason to believe that income had escaped

assessment in as much as the information showed that the industrial undertaking was in existence prior to the date of the lodging of the claim for

deduction u/s 80IB of the Act by the assessee for asst. yr. 2001-02.

8. Two petitions under Article 226 of the Constitution have been instituted by the assessee to challenge the reopening of the assessment for asst.

yrs. 2003-04 and 2004-05. The assessment for asst. yr. 2003-04 has been reopened beyond a period of four years after the expiry of the relevant

assessment year. The reopening of assessment for asst. yr. 2004-05 is within a period of four years from the expiry of relevant assessment year.

The case for asst. yr. 2004-05 will be considered separately in the later part of the judgment.

9. On behalf of the petitioner, it was urged before the Court by learned Counsel that : (i) There was no failure on the part of the assessee to

disclose all material facts relevant to the assessment. The license was filed when assessment proceedings took place for asst. yr. 2003-04. A full

enquiry was made and all relevant details were disclosed. The license contains a disclosure of the circumstance that plans had been approved on

12th Sept., 1988; (ii) In any event, there was no connection between the alleged non-disclosure and the conclusion formed by the AO. Even if it

were to be assumed that a factory had been worked at the site by the person who was subjected to proceedings under State Financial

Corporations Act, 1961 by MSFC, that would not disentitle the petitioner to the benefit of a deduction u/s 80IB of the Act. The petitioner who

has set up a new industrial undertaking by purchasing plant and machinery would still be entitled to a deduction u/s 80IB of the Act; (iii) The

reasons for reopening an assessment must indicate both a failure to disclose all material facts and what circumstance constitutes the failure to

disclose. In the present case, that requirement has not been fulfilled; (iv) In the present case, the AO had not formed the belief that income had

escaped assessment. The information which has been obtained under the Right to Information Act would reveal that the action had been instituted

merely on the basis of an audit report; (v) The benefit of a deduction u/s 80IB was granted for asst. yrs. 2001-02 and 2002-03, where the

assessment orders have attained finality. Unless the deduction for the first year was withdrawn in accordance with law, the relief for the subsequent

years cannot be withheld.

10. Insofar as the companion writ petition is concerned, as noted earlier, the assessment has been reopened within a period of four years of the

expiry of the relevant assessment year. In that case, it has been urged that the reopening of the assessment amounts to a case of a change of

opinion. No material was available before the AO to come to the conclusion that the income had escaped assessment, having regard to the fact

that for the earlier assessment years, the assessment had been completed after the assessee had placed on record all the circumstances including

the fact that the plans had been approved on 12th Sept., 1988. It was urged that there was no reason to believe that income had escaped

assessment since it is only on the basis of an audit objection that the assessment was sought to be reopened. Finally, it was urged that the Revenue

was not entitled to reopen the assessment for asst. yr. 2004-05, once the assessment for the earlier years had attained finality.

11. On behalf of the Revenue, it has been submitted, based on the reply, that during the course of the subsequent proceedings a copy of the license

was filed by the petitioner which states that the plan for the factory had been approved by the Sarpanch on 12th Sept., 1988. This information,

according to the Revenue, was not produced during the course of the assessment proceedings for the earlier years. The information showed that

the industrial undertaking was in existence much before the date of the lodging of the claim u/s 80IB of the Act for asst. yr. 2001-02. According to

the Revenue, the industrial unit was already in existence and was in use of some other person for the purposes of availing the benefit u/s 80IB of

the Act.

12. Section 147 provides that if the AO has reason to believe that any income chargeable to tax has escaped assessment for any assessment year,

he may, subject to the provisions of Sections 148 - 153 assess or reassess such income and also any other income chargeable to tax which has

escaped assessment and which comes to his notice subsequently in the course of the proceedings under the section. Under the first proviso, where

an assessment has been made under Sub-section (3) of Section 143 or Section 147 for the relevant assessment year, no action can be initiated u/s

147 after the expiry of four years from the end of the relevant assessment year unless the income chargeable to tax has escaped assessment by

reason of the failure of the assessee inter alia to disclose fully and truly all material facts necessary for his assessment, for that assessment year. The

jurisdictional condition u/s 147 is the formation of belief by the AO that income chargeable to tax has escaped assessment for any assessment year.

The reasons which are recorded by the AO are crucial and it is on the basis of those reasons alone that the validity of the order reopening an

assessment has to be decided. Where an assessment has been made u/s 143(3), action can be initiated after the expiry of four years from the end

of the relevant assessment year if the income chargeable to tax has escaped assessment because of the failure of the assessee to make fully and

truly a disclosure of the material facts. The provisions of Section 147 have been interpreted in a recent judgment of the Supreme Court in

Commissioner of Income Tax, Delhi Vs. Kelvinator of India Limited, . The Supreme Court noted that after 1st April, 1989, the power to reopen is

much wider than earlier since the substantive part of Section 147 only imposes one condition namely that the AO must have reason to believe that

income has escaped assessment. The Supreme Court held that nonetheless, a mere change of opinion would not justify the exercise of the power

to reopen an assessment and there must be tangible material before the AO to come to the conclusion that income has escaped assessment. The

Supreme Court held thus:

...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 AO 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 AO has no power to review; he has the power to

reassess. But reassessment has to be based on fulfilment of certain precondition 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 inbuilt test to check abuse of power by the AO. Hence, after 1st April, 1989, AO has power to reopen, provided there is ''tangible

material'' to come to the conclusion that there is escapement of income from assessment. Reasons must have a live link with the formation of the

belief.

13. The assessee made a claim for deduction u/s 80IB of the Act, initially for asst. yr. 2001-02, which was allowed. The benefit of a deduction u/s

80IB was also granted for asst. yr. 2002-03. The assessment order for asst. yr. 2001-02 was passed u/s 143(3) of the Act, upon scrutiny. During

the course of assessment proceedings for asst. yr. 2003-04, the assessee filed an audit report in Form 10CCB in which relevant particulars of the

license to work that was granted to the unit of the assessee was disclosed. The license to work dt. 14th Aug., 2000, copy of which was filed

before the AO, contains a disclosure of the fact that the plans have been approved by the Sarpanch by his letter dt. 12th Sept., 1988. The basis on

which the assessment for asst. yrs. 2003-04 and 2004-05 has been sought to be reopened is that it was during the course of assessment

proceedings for subsequent years that the Revenue had obtained a copy of the license which showed that the plans have been approved as far

back as on 12th Sept., 1988. This statement which is contained in the reasons, on the basis of which the assessment is sought to be reopened, is

belied by the record which shows that the Revenue was in possession of the material produced by the assessee during the course of the

assessment proceedings for asst. yr. 2003-04 which showed that the plans had been approved in the year 1988. Therefore, the basis on which the

assessment has been sought to be reopened is factually incorrect. The AO granted the assessee a deduction u/s 80IB after being appraised of all

the relevant details, including those in Form 10CCB which showed that plans had been approved in 1988.

14. Moreover, the fact that plans for the building were approved in the year 1988 would make no difference to the claim of the assessee to a

deduction u/s 80IB of the Act. Both in the notice reopening the assessment and in the order disposing of the objections of the assessee, reliance

has been sought to be placed on the provisions of Sub-clause (i) of Clause (1) of Sub-section (2) of Section 80IB. Sub-Clause (i) postulates that

the industrial undertaking ought not to have been formed either by splitting up or reconstruction of a business already in existence. On the basis of

the facts and circumstances and as recorded by the AO, it cannot possibly be postulated that the industrial undertaking of the assessee was formed

either by the splitting up or by the reconstruction of a business already in existence. As already noted, it is an admitted position that the land and

building was sold by MSFC in exercise of its statutory powers and the purchaser in turn has leased out the land and building to the assessee. It is

not the case of the Revenue in the reasons for reopening the assessment that the plant and machinery installed by the assessee has been previously

used. Section 80IB(2)(ii) provides that the industrial undertaking should not be formed by transfer to a new business of plant and machinery or a

plant previously used for any other purpose. It is not the case of the Revenue in the reasons for reopening the assessment that the industrial

undertaking of the assessee has been formed by transfer of plant and machinery which has been previously used for any other purpose. The

assessee has annexed to the petition before the Court a copy of the deed of conveyance under which MSFC transferred the right of the defaulter

only in respect of the land and building. The plant and machinery was not the subject-matter of the sale. The deed of conveyance contains a

specific recital that the machinery was not being sold. In these circumstances, it is apparent from the record before the Court that there was no

failure on the part of the assessee to disclose fully and truly all the material facts necessary for the assessment so as to justify the invocation of the

powers u/s 148 of the Act beyond the expiry of a period of four years from the end of the relevant assessment year.

15. We may also note in addition that the assessee has filed together with its affidavit in rejoinder, a copy of the information received during the

course of a query under the Right to Information Act. The information includes a letter by the AO to the CIT dt. 24th March, 2009 seeking

permission to the proposal for reopening the assessment u/s 151(1) of the Act. The AO has noted, while seeking approval of the CIT, that during

the course of revenue audit proceedings, an audit objection has been raised on the ground that the assessee was not eligible to a deduction u/s

80IB from asst. yr. 2002-03. The AO notes that the audit objection was not accepted but that as a precautionary measure the assessment was

reopened u/s 147. There is merit in the submission urged on the part of the assessee that the AO had no reason to believe that income had

escaped assessment. We clarify that we have not regarded this circumstance namely, the information which was divulged during the course of a

query and the Right to Information Act as the only and exclusive circumstance for coming to a conclusion that the power has not been validly

exercised. Basically, the validity of the exercise of the powers to reopen an assessment has to be decided with reference to the reasons recorded

while reopening the assessment. The reasons recorded while reopening the assessment do not justify the exercise of the power in the facts of this

case.

16. Insofar as the companion writ petition is concerned (Writ Petn. No. 268 of 2010), the reopening of the assessment has taken place within a

period of four years from the expiry of the relevant assessment year. However, so far as this case is concerned, it is apparent that the AO did not

have before him any additional material at all to form a belief that income had escaped assessment. The assessee had admittedly placed on record

before the AO for asst. yr. 2003-04 the circumstance that the plans have been approved for the building on 12th Sept., 1988. There was no

material before the AO, that would lead to a formation of belief that the income had escaped assessment. We may also note that in the present

case as well the AO appears to have relied exclusively on an audit objection, which has already been dealt with while considering the facts of Writ

Petn. No. 269 of 2010. There was hence a total absence of ""tangible material"", as explained in the judgment of the Supreme Court in Kelvinator

(supra) to justify the conclusion that income had escaped assessment. Finally, it would be necessary to note, as we have observed earlier, that

mere existence of the land and building since 1988 is not a circumstance which would disentitle the assessee to the benefit of a deduction u/s 80IB

of the Act, once other requirements of the provisions are fulfilled.

17. For all these reasons, we quash and set aside the notices dt. 24th March, 2009 and 31st March, 2009. Rule is made absolute accordingly. In

the circumstances of the case, there shall be no order as to costs.