

(2008) 04 KAR CK 0039

In the Karnataka High Court

Case No : Income Tax Appeal No's. 102, 105 and 106 of 2002

Commissioner of Income Tax and Another

APPELLANT

Vs

Dr. N. Thippa Setty

RESPONDENT

Date of Decision : 09-04-2008

Acts Referred:

Income Tax Act, 1961 — Section 132, 148, 148 (2), 260 A

Citation : (2010) 230 CTR 265

Hon'ble Judges : Deepak Verma, J;Anand Byrareddy, J

Bench : Division Bench

Advocate : M.V. Seshachala, for the Appellant; A. Shankar, for the Respondent

Final Decision : Allowed

Judgement

Deepak Verma, J.—Heard Sri M.V. Seshachala, learned Counsel for the appellants and Sri A. Shankar, learned Counsel for the respondent. This order shall also govern disposal of IT Appeal Nos. 105 of 2002 and 106 of 2002, which are for the asst. yrs. 1989-90, 1990-91 and 1993-94 respectively arising out of common order passed by Tribunal. It has not been disputed before us that in all the aforesaid appeals, which are at the instance of the Revenue, common questions of law have been formulated, which are required to be adjudicated, by this Court.

2. These appeals u/s 260A of the IT Act, 1961 (hereinafter shall be referred to in short as "the Act") are at the instance of Revenue against the order dt. 30th Oct., 2001 passed by the Tribunal, Bangalore Bench "C" in ITA Nos. 545 to 552/Bang/2000 for the aforesaid assessment years. The appeals before the Tribunal were at the instance of the assessee against the consolidated order passed by the CIT(A) on 5th June, 2000, for the same assessment years.

In fact out of the impugned order passed by the Tribunal, eight appeals were preferred by the Revenue. Out of those eight appeals, three appeals already stood disposed of by an earlier order passed by this Court. IT Appeal Nos. 99 of 2002 and 101 of 2002 for the asst. yrs. 1991-92 and 1992-93 have been

disposed of by us yesterday, as the original records produced before us categorically revealed that there has not been any mandatory compliance with regard to Section 148(2) of the Act in as much as no reasons have been recorded for invoking the said section. Thus on technical ground, those two appeals have been disposed of, without going into merits of the same.

3. Although several substantial questions of law have been formulated by the learned Counsel for the Revenue in the appeals, but vide order dt. 9th Feb., 2004 the questions of law have been reframed and the appeals have been admitted only on the reframed substantial questions of law, which are as under:

1. Whether the Tribunal was correct in holding that the statements given by the assessee on oath during search could not be used as evidentiary value in assessment, as the assessee had retracted these statements?
2. Whether the Tribunal was correct in holding that reopening of assessment is based on mere suspicion and without any material as the confession made by the assessee during search was withdrawn before issue of notice u/s 148 of the Act and consequently the assessment was liable to be cancelled?
3. Whether the Tribunal was correct in holding that the undisclosed income from money-lending business and unexplained investments in the fixed deposits cannot be assessed in the hands of the assessee?
4. Whether the Tribunal was correct in deleting the additions made by the AO in respect of unexplained credits and repayment of loan not accounted for?

Thus we are required to address on the aforesaid substantial questions of law.

4. The facts of the case, lie in narrow compass, which are mentioned hereinbelow:

A search was conducted in the residential premises of the assessee on 23rd Aug., 1994, purportedly exercising the power conferred on the Department u/s 132 of the Act. The assessee is a medical practitioner and is assessed to tax in the status of individual deriving the income by way of insurance commission, income from house property, etc. During the course of search, the following valuables were seized by the Department:

(i) Cash Rs. 9,00,000 (ii) Pawned gold Rs. 9,47,584 (iii) Pledged NSCs. Rs. 45,70,843 (iv) FDRs. Rs. 9,24,300

It has not been disputed before us that pursuant to the search conducted in the premises of the assessee, he had made declaration/statement u/s 132(4) of the Act on 23rd Aug., 1994 and again on 28th Sept., 1994. He later on retracted the said statements mentioning therein that the same obtained under duress and coercion and he did not understand the implication of the same. In the letter of retraction addressed by the assessee to the Department, he further went on to state that on the dates of his recording statements, he was not keeping well. Retractions were made by the assessee on 18th Oct., 1994 and 7th Dec, 1994.

By the later retraction he further elaborated the circumstances under which he was required to make earlier statement u/s 132(4) of the Act and reiterated his prayer for retraction thereof.

Rejecting his request that the declaration was not voluntary, an order u/s 132(5) came to be passed retaining the assets seized on 23rd Aug., 1994 as the assets of the assessee and adding it to the income of the assessee, objected to the said order.

The Department had completed the assessment u/s 143(1) for the asst. yrs. 1986-87 to 1988-89 after accepting the returns. For the asst. yrs. 1989-90 to 1993-94 the original returns filed by the assessee were processed u/s 143(1)(a) of the Act accepting the same.

After discovery of the aforesaid documents during the course of search and seizure, the assessments were reopened by the Asstt. CIT (Inv.), Circle 1(1), after recording reasons on 5th Oct., 1995. The assessee was thereafter issued notice u/s 148 of the Act. For the asst. yrs. 1989-90 and 1990-91 the following reasons have been recorded u/s 148(2) of the Act, which are reproduced hereinbelow:

Asst. yr. 1989 90

The assessee has offered in his statement u/s 132(4) the interest income earned by him of Rs. 26,638 and also investments made by him in fixed deposit of Rs. 40,696 for the asst. yr. 1989-90.

In view of the above facts, I have reasons to believe that the interest income and investments made in fixed deposit to the tune of Rs. 67,334 has escaped assessments within the meaning of Section 147.

Proposal to the Dy. CIT, put up u/s 147 for the issue of notice u/s 148.

Except for some minor changes as mentioned hereinabove, similar reasons have been recorded by the authority for the asst. yr. 1990-91.

However, for the asst. yr. 1993-94 the following reasons have been recorded by the AO on 12th Aug., 1994 which read as thus:

I have reasons to believe that the income chargeable to tax has escaped assessment for the asst. yr. 1993-94.

Notice u/s 148, put up.

5. The AO thereafter completed the assessment after making various additions. Feeling aggrieved by the said additions made in the income of the assessee, he was constrained to file appeals before the CIT(A). The appellate authority also did not accept the plea of the assessee and proceeded to reject the appeals on merits.

6. Further feeling aggrieved by the said orders passed by the CIT(A), he was

constrained to prefer appeals before the Tribunal. The said appeals having been allowed by the Tribunal and the findings having been recorded in favour of the assessee, now these appeals are before us at the instance of Revenue, as mentioned hereinabove u/s 260A of the Act.

7. We have accordingly heard learned Counsel for parties at length and perused the records.

8. The basic and foremost question that crops up for consideration before this Court is as to what will be the evidentiary value of the statements of the assessee, recorded u/s 132(4) of the Act, which were admittedly retracted by him, even before issuance of notice to him u/s 148 of the Act.

9. Learned Counsel for the appellants-Revenue Sri M.V. Seshachala submitted that once the statement was given by the assessee, there is no provision in the Act to retract the same. Hence the Tribunal could not have proceeded on the basis that assessee had retracted his statements given u/s 132(4) of the Act. He further contended that after the amendment of Section 147 w.e.f. 1st April, 1989, sufficiency or otherwise of the reasons recorded could not be allowed to be enquired into. According to him if there existed prima facie material to reopen the case, the same would be sufficient for the Revenue to commence reassessment proceedings. It was also contended that looking to the voluminous incriminating documents found at the time of search and seizure, there was sufficient material before the Revenue for issuance of notice u/s 148 of the Act. The findings recorded by the Tribunal are also being attacked and criticised on variety of grounds.

10. Per contra, Sri A. Shankar, learned Counsel appearing for the assessee contended that once the statement given by the assessee u/s 132(4) of the Act was withdrawn or retracted, the same could not be a basis for reopening the proceedings as contemplated under Sections 147 and 148 of the Act. He further contended that de hors the statements of the assessee, retracted subsequently there was nothing before the AO for reopening of the cases. It has also been contended that it was done before issuance of notice u/s 148 of the Act. It was also contended that in any case, the AO was fully aware that the statements have been retracted by the assessee and thus if at all he wanted to proceed against the assessee, some other reason should have been recorded by him for reopening. He would therefore contend that the very issuance of notice u/s 148 of the Act, to the assessee was invalid. If that be so, then all subsequent proceedings initiated on the strength of the said notice would automatically fail and nothing can survive if the reasoning are held to be insufficient for reopening of the assessment.

11. Initially at the time of hearing there was some dispute whether assessee had in fact retracted his statements or not but the same has been set at rest by the letter addressed by the assessee to the Asstt. CIT dt. 23rd March, 1998 in which he has categorically stated that the declaration obtained u/s 132(4) of the Act

was withdrawn and the same is not in force. Tenor of this letter shows that even before issuance of this letter he had already retracted his statement u/s 132 of the Act. In fact, similar prayer was already made by the assessee as far back as on 7th Dec, 1994. Since cognizance of this retraction had not been taken by the AO, assessee was constrained to approach the Dy. CIT for necessary direction u/s 144A of the Act. On this, an order came to be passed by the CIT on 16th March, 1998 and the AO was issued the following directions:

(a) to afford another opportunity of being heard to the assessee before finalising reassessment proceedings with reference to the disclosure made u/s 132(4) and seized material, etc., and complete the said assessment for the said assessment year on the basis of his finding;

(b) in case the assessee fails to furnish satisfactory evidence in support of his retraction of disclosure u/s 132(4) notwithstanding another opportunity provided to him [vide (a) above], the AO is directed to complete the reassessment for the assessment year as per his proposal vide reference above. The assessee has undertaken to furnish all particulars on or before 23rd March, 1998.

12. The AO thereafter passed the order on 27th March, 1998. Since these directions were given to the AO, it can safely be presumed that he was fully aware of the said order passed by the Dy. CIT, Hubli. However, the order passed by the AO shows that there is no whisper with regard to the retraction of the statement made by the assessee and compliance of the directions as contained in the order passed by the Dy. CIT. The order passed by the AO on 27th March, 1998 has been filed as per Annex. "C". In the light of the aforesaid fact situation, we have to examine as to what would be the legal position after retraction of the statements by the assessee, and still after retraction, there existed sufficient material or reasons to reopen the case or not.

13. Learned Counsel for the Revenue has placed reliance on the following judgments of the Supreme Court and High Courts:

- (i) Surjeet Singh Chhabra Vs. Union of India and others,
- (ii) Greenview Restaurant Vs. Assistant Commissioner of Income Tax,
- (iii) Ramjas Nawal v. CIT (2003) 183 CTR (Raj) 144

Critical examination of the aforesaid judgments, would show that they deal with the aspect of retraction of statements, recorded earlier.

14. We have already discussed, in the preceding paras, wherein it is crystal clear that the statements made by the assessee u/s 132(4) of the Act were retracted not once, but twice. Since cognizance of retraction was not being taken by the AO, he was constrained to move the Dy. CIT for redressal of his grievance u/s 144A of the Act, wherein certain directions were given to the AO. In view of the aforesaid factual aspect, it leaves no amount of doubt in our mind that the assessee had already retracted the statements, which were also accepted by the

Department. Thus the aforesaid judgments which deal with question of retraction are not required to be discussed any more as on facts it is established, in the case in hand that assessee had retracted his statements.

15. With regard to the reopening of assessment u/s 148 of the Act, learned Counsel for the appellant has placed reliance on the following judgments of the Supreme Court:

(i) S. Narayanappa and Others Vs. Commissioner of Income Tax, Bangalore,

(ii) Assistant Commissioner of Income Tax Vs. Rajesh Jhaveri Stock Brokers Pvt. Ltd.,

(iii) GKN Driveshafts (India) Ltd. Vs. Income Tax Officer and Others,

16. In the case of S. Narayanappa (supra), Supreme Court dealing with Section 34(1)(a) of the IT Act, 1922, has held as under:

The expression "reason to believe" in Section 34 does not mean a purely subjective satisfaction on the part of the ITO. The belief must be held in good faith; it cannot be merely a pretence. It is open to the Court to examine 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.

17. It has been further held in the said judgment that those reasons must be sufficient for a prudent man to come to the conclusion that the income had escaped assessment. In this regard, it has been held that two of the following conditions must be fulfilled before case is sought to be reopened, namely : (1) the first condition is that the ITO must have reason to believe that the income, profits or gains chargeable to Income Tax had been underassessed; (2) the second condition is that he must have reason to believe that such "underassessment" had occurred by reason of either, (i) omission or failure on the part of an assessee to make a return of his income u/s 22, or (ii) omission or failure on the part of the assessee to disclose fully and truly all the material facts necessary for his assessment for that year.

18. The Supreme Court then further went on to hold that fulfillment of the same is condition precedent to be satisfied by the AO, before he acquires jurisdiction to issue a notice under this Act.

19. In the matter of Rajesh Jhaveri (supra), the Supreme Court while dealing with the provisions of Sections 147 and 148 of the Act, has held as under:

Section 147 authorises and permits the AO to assess or reassess income chargeable to tax if he has reason to believe that income for any assessment year has escaped assessment. The word "reason" in the phrase "reason to believe" would mean cause or justification. If the AO has cause or justification to know or suppose that income had escaped assessment, it can be said to have reason to believe that an income; had escaped assessment. The expression

cannot be read to mean that the AO should have finally ascertained the fact by legal evidence or conclusion. The function of the AO is to administer the statute with solicitude for the public exchequer with an in-built idea of fairness to taxpayers.

20. The last judgment of the Supreme Court in the case of GKN Drive shafts (India) Ltd. v. ITO and Ors. (supra), does not deal with the reasons to be assigned by the AO for reopening of the case, but proceeds to hold that once the case has been reopened and notice to the assessee has been issued u/s 148 of the Act, then he shall have a right to ask for reason for reopening and then challenge the same in accordance with law.

21. As against these judgments, learned Counsel for the assessee has placed reliance on the following judgments of various High Courts and the Supreme Court:

- (i) Income Tax Officer and Others Vs. Madnani Engineering Works Ltd., Calcutta,
- (ii) Birla Vxl Ltd. Vs. Assistant Commissioner of Income Tax,
- (iii) H. Noronha Vs. Income Tax Officer, Circle-II, Bangalore,
- (iv) Chhugamal Rajpal Vs. S.P. Chaliha and Others,
- (v) EQUITABLE INVESTMENT CO. (P.) LTD. Vs. Income Tax OFFICER, G. WARD, AND OTHERS.,
- (vi) Hindustan Lever Ltd. Vs. R.B. Wadkar, Assistant Commissioner of Income Tax and Others (No. 1),
- (vii) Indian Oil Corporation Vs. Income Tax Officer, Calcutta and Others,
- (viii) Ganga Saran and Sons P. Ltd. Vs. Income Tax Officer and Others,
- (ix) Unreported judgment of this Court passed by learned Single Judge in Writ Petn. No. 11573 of 1989 (decided on 11th Jan., 1991) A. Nagappa v. Asstt. CIT;
- (x) Appellate judgment passed by the Division Bench in Writ Appeal No. 928 of 1991 (decided on 19th March, 1992) Asstt. CIT v. A. Nagappa.

22. In the matter of Madnani Engineering Works Ltd. (supra), it has been held as under by the apex Court:

We may also point out that though it was contended in the writ petition that the ITO could have no reason to believe that any part of the income of the respondent had escaped assessment by reason of its failure to make a full and true disclosure of material facts, the ITO did not disclose in his affidavit any material on the basis of which it could be said that he had come to the requisite belief. All that the ITO stated in his affidavit was that he discovered that the transactions of loan against security of Hundis were not genuine and that the credits against the names of certain persons who were alleged to have advanced

loans were bogus.

It was further held as under:

We are, therefore, not at all satisfied on the affidavit that the ITO had reason to believe that a part of the income of the respondent had escaped assessment by reason of its failure to make a true and full disclosure of the material facts.

23. Gujarat High Court in the matter of Birla VXL Ltd. (supra) has dealt with the issue as under:

"Why" for holding such belief must be reflected from the record of reasons made by the AO. In a case where the AO holds the opinion that because of excessive loss or depreciation allowance income has escaped assessment, the reasons recorded by the AO must disclose by what process of reasoning he holds such a belief that excessive loss or depreciation allowance has been computed in the original assessment. Merely saying that excessive loss or depreciation allowance has been computed without disclosing the reasons which led the assessing authority to hold such a belief, in our opinion, does not confer jurisdiction on the AO to take action under Sections 147 and 148 of the Act.

24. This Court in the matter of H. Noronha (supra), has held that mere suspicion would not be sufficient for reopening of the case unless there existed some other prima facie evidence to warrant reopening.

25. In the matter of Chhugamal Rajpal (supra), apex Court while considering the reasons assigned by the AO, in its inimitable way has held as under:

Hence proper investigation regarding these loans is necessary. In other words his conclusion is that there is a case for investigating as to the truth of the alleged transactions. That is not the same thing as saying that there are reasons to issue notice u/s 148. Before issuing a notice u/s 148, the ITO must have either reasons to believe that by reason of the omission or failure on the part of the assessee to make a return u/s 139 for any assessment year to the ITO or to disclose fully and truly all material facts necessary for his assessment for that year, income chargeable to tax has escaped assessment for that year or alternatively notwithstanding that there has been no omission or failure as mentioned above on the part of the assessee, the ITO has in consequence of information in his possession reason to believe that income chargeable to tax has escaped assessment for any assessment year.

26. Calcutta High Court in the matter of Equitable Investment Co. (P) Ltd. (supra), has examined all the previous judgments of the Supreme Court and the High Court on the issue, to come to the following conclusion:

Accordingly, in our opinion, it is not open to the CIT to support the notice u/s 148 on the basis of material which does not find place in the report.

27. Confronted with identical fact situation, Bombay High Court in the matter of Hindustan Liver Ltd. (supra) has held as under:

It is needless to mention that the reasons are required to be read as they were recorded by the AO. No substitution or deletion is permissible. No additions can be made to those reasons. No inference can be allowed to be drawn/based on reasons not recorded. It is for the AO to disclose and open his mind through reasons recorded by him. He has to speak through his reasons. It is for the AO to reach the conclusion as to whether there was failure on the part of the assessee to disclose fully and truly all material facts necessary for his assessment for the concerned assessment year. It is for the AO to form his opinion. It is for him to put his opinion on record in black and white. The reasons recorded should be clear and unambiguous and should not suffer from any vagueness. The reasons recorded must disclose his mind. The reasons are the manifestation of the mind of the AO. The reasons recorded should be self-explanatory and should not keep the assessee guessing for the reasons. Reasons provide the link between conclusion and evidence. The reasons recorded must be based on evidence. The AO, in the event of challenge to the reasons, must be able to justify the same based on material available on record. He must disclose in the reasons as to which fact or material was not disclosed by the assessee fully and truly necessary for assessment of that assessment year, so as to establish the vital link between the reasons and evidence. That vital link is the safeguard against arbitrary reopening of the concluded assessment.

28. The Supreme Court in the matter of Indian Oil Corporation (supra) has held:

But reason to believe is not the same thing as reason to suspect.

29. Now coming to the Single Bench judgment of this Court in the matter of A. Nagappa, wherein the reasons of the AO, were elaborate, were reproduced. Yet it proceeded to quash the notice issued to the assessee u/s 148 of the Act. This order was the subject-matter of challenge at the instance of Revenue in Writ Appeal No. 928 of 1991 before the Division Bench of this Court, which held as under:

More than the Addl. Director of IT's report which the learned Judge characterised as evasive and speculative, it is the statement of reasons for the reopening which is evasive and speculative, We find no basis therein which could have led the appellant to entertain reasons to believe that income chargeable to tax had escaped assessment for the relevant assessment year. It is imperative that the reasons should have a rational and relevant nexus to the formation of such belief. We do not find such nexus.

30. The Supreme Court had the occasion to consider this aspect of the matter in Ganga Saran & Sons (P) Ltd. (supra), wherein it has dealt with the situation beautifully by holding as under:

It is well-settled as a result of several decisions of this Court, that two distinct conditions must be satisfied before the ITO can assume jurisdiction to issue notice u/s 147(a). First, he must have reason to believe that the income of the assessee has escaped assessment, and secondly, he must have reason to believe

that such escapement is by-reason of the omission or failure on the part of the assessee to disclose fully and truly all material facts necessary for his assessment. If either of these conditions is not fulfilled, the notice issued by the ITO would be without jurisdiction. The important words u/s 147(a) are "has reason to believe" and these words are stronger than the words "is satisfied". The belief entertained by the ITO must not be arbitrary or irrational. It must be reasonable or in other words it must be based on reasons which are relevant and material.

31. In the light of the aforesaid judgments of various High Courts and Supreme Court, we have examined whether there existed sufficient reasons for reopening of the case against the assessee, exercising the power conferred on the AO u/s 148 of the Act. The reasons to believe have been reproduced by us as recorded by the AO. The same would show that he was not even able to find out prima facie case with regard to the escaped assessment within the meaning of Section 147 of the Act.

32. For the asst. yr. 1993-94 in fact no cogent and valid reasons have been assigned by the AO for reopening of the case. In the light of the aforesaid discussions, we have no hesitation to hold that there existed no material for reopening of the case against the assessee.

33. It is further pertinent to mention here that once the statements said to have been recorded u/s 132(4) of the Act were withdrawn, then there existed no material on record to warrant reopening of the case against the assessee u/s 148 of the Act. If the very basis on which reopening was ordered did not exist, there was no question for reopening of the case. This material aspect of the matter has not been considered by the AO, who proceeded to direct reopening of the case, without there being any legally admissible evidence available on record. Thus the very issuance of notice u/s 148 of the Act is found to be illegal and absolutely without jurisdiction.

34. Learned Counsel for the respondent also contended that even on merits. Revenue would not have been justified to issue such a notice especially in the light of the affidavits submitted by the brothers of the assessee; mentioning categorically therein that several fixed deposits, and other funds which have been added to the income of the assessee, in fact belonged exclusively to them. This is what they had submitted in the affidavits submitted before the authorities of the Department. Since even after taking those amounts in their individual names, the income did not cross the taxable limits, they did not file any returns. But Revenue also did not issue any notices to them.

35. However, since we are not going into merits of the matter and only on this preliminary issue we decide the questions in appeals in favour of the assessee and against the Revenue. We accordingly hold that: there existed no good or sufficient grounds or reasons for reopening of the case u/s 148 of the Act against the assessee.

36. In view of this, we find that there is no merit or substance in this appeal and the connected appeals. Accordingly we dispose of this and the connected appeals.