

(1999) 06 BOM CK 0009
In the Bombay High Court
Case No : I. T. R. No. 497 of 1987

Commissioner of Income Tax, Bangalore	APPELLANT
Vs	
Hade Navigation (P) Ltd., Goa	RESPONDENT

Date of Decision : 22-06-1999

Acts Referred:

Income Tax Act, 1961 — Section 125, 125A, 139, 143, 143(2)

Citation : (2000) 3 BomCR 396 : (1999) 157 CTR 355 : (1999) 239 ITR 726 : (1999) 3 MhLj 575 : (1999) 107 TAXMAN 372

Hon'ble Judges : Ranjana Desai, J;B. P. Saraf, J

Bench : Division Bench

Advocate : R. V. Desai with P. S. Jetly instructed by T. C. Kaushik, for the Appellant; S. M. Inamdar with P. Vaidya, for the Respondent

Judgement

Dr. B. P. Saraf, J.—By this reference u/s 256(1) of the income tax Act, 1961. the income tax Appellate Tribunal has referred the following questions of law to this Court for opinion :

At the instance of revenue :

"1. Whether, on the facts and in the circumstances of the case the Tribunal was right in law in holding that the second draft assessment order was invalid in law and, therefore, the disallowance of investment allowance in the second draft assessment order has to be ignored?" At the instance of assessee :

"2. Whether, on the facts and in the circumstances of the case, the Tribunal was correct in holding that there was a transfer of the ship to the Insurance Company when the ship became a dead loss and capital gains was leviable on the assessee receiving compensation from the Insurance Company in respect of destruction of the ship?"

2. This reference pertains to the assessment year 1978-79. The material facts giving rise to reference of question No.1 are as follows :-

The assessee, a private limited company, submitted its return of income for the assessment year 1978-79 with the income tax Officer u/s 139 of the income tax Act, 1961 ("Act"). In compliance to notice issued u/s 143(2) of the Act, the assessee appeared before the income tax Officer and produced evidence in support of its return. After taking into account the relevant material available with him, the income tax Officer made an assessment of the total income of the assessee u/s 143(3) of the Act. As the proposed variation in the income returned by the assessee exceeded the amount of Rs. 1,00,000/-, the income tax Officer forwarded a draft assessment order ("draft order") to the assessee as required by section 144B of the Act. This was done on 3rd March 1981. From the statement of case, it appears that no objection was filed by the assessee within seven days of the receipt of the draft order nor any application was made for extension of time for that purpose. Despite that, the income tax Officer did not complete the assessment on the basis of the draft order. On the other hand, on 23rd March, 1981, i.e. 10 days after the service of the draft order on the assessee, he forwarded another draft order to the assessee. In the second draft order, the income tax Officer disallowed the investment allowance of Rs. 13,76,350/- claimed by the assessee which he had allowed in the first draft order. As a result, the assessed income of the assessee was enhanced to that extent. The variation of the returned income was also enhanced by Rs. 13,76,350/-. The assessee challenged the powers of the income tax Officer to issue second draft order. This objection of the assessee was overruled and the assessment was finalised by the income tax Officer in terms of the second draft order. The assessee appealed to the Commissioner of income tax (Appeals). The Commissioner (Appeals) dismissed the appeal of the assessee and upheld the view taken by the income tax Officer. While doing so, the Commissioner (Appeals) relied upon the decision of the Madhya Pradesh High Court in *Banarsidas Bhanot and Sons Vs. Commissioner of Income Tax*, . The assessee went in further appeal before the income tax Appellate Tribunal ("Tribunal"). The Tribunal accepted the contentions of the assessee and held that the second draft order of the income tax Officer was bad in law. The Tribunal followed the decision of the Delhi High Court in *Sudhir Sareen Vs. Income Tax Officer, Central Circle XVII, New Delhi* and another, . Aggrieved by the above decision of the Tribunal, revenue is before us by way of reference of question No. 1 for our opinion:

3. We have heard Mr. R. V. Desai, learned counsel for the revenue, who submits that the Tribunal erred in law in holding that the income tax Officer had no power to forward second draft order. In support of this contention, he relied upon decision of the Madhya Pradesh High Court in *Banarsidas Bhanot & Sons vs. C.I.T.* (supra) and the decision of Calcutta High Court in *Shahdara (Delhi) Saharanpur Light Railway Co. Ltd. (in voluntary liquidation) Vs. Commissioner of Income Tax*, . According to Mr. Desai, the decision of Delhi High Court in *Sudhir Sareen vs. I.T.O.* (supra) does not lay down the correct law and, therefore, should not be followed. The learned counsel for the assessee, on the other hand, relies on the decision of the Delhi High Court in *Sudhir Sareen vs. I. T. O.* (supra)

and submits that the income tax Officer can submit only one draft order to the assessee u/s 144B of the Act and if the assessee does not forward any objection within seven days from the receipt of the draft order or extended period, the draft assessment order becomes final u/s 143(3).

4. We have considered the rival submissions of the learned counsel for the parties. Section 144B of the Act, as it stood at the material time, reads as follows :

"144B. Reference to Inspecting Assistant Commissioner in certain cases.-(1) Notwithstanding anything contained in this Act, where in an assessment to be made under sub-section (3) of section 143, the income tax Officer proposes to make any variation in the income or loss returned which is prejudicial to the assessee and the amount of such variation exceeds the amount fixed by the Board under subsection (6), the income tax Officer shall, in the first instance, forward a draft of the proposed order of assessment (hereinafter in this section referred to as the draft order) to the assessee.

(2) On receipt of the draft order, the assessee may forward his objections, if any, to such variation to the income tax Officer within seven days of the receipt by him of the draft order or within such further period not exceeding fifteen days as the income tax Officer may allow on any application made to him in this behalf.

(3) If no objections are received within the period or the extended period aforesaid or the assessee intimates to the income tax Officer the acceptance of the variation, the income tax Officer shall complete the assessment on the basis of the draft order.

(4) If any objections are received, the income tax Officer shall forward the draft order together with the objections to the Inspecting Assistant Commissioner and the Inspecting Assistant Commissioner shall, after considering the draft order and the objections and after going through (wherever necessary) the records relating to the draft order, issue, in respect of the matters covered by the objections, such directions as he thinks fit for the guidance of the income tax Officer to enable him to complete the assessment:

Provided that no directions which are prejudicial to the assessee shall be issued under this sub-section before an opportunity is given to the assessee to be heard.

(5) Every direction issued by the Inspecting Assistant Commissioner under sub-section (4) shall be binding on the income tax Officer.

(6) For the purposes of sub-section (1), the Board may, having regard to the proper and efficient management of the work of assessment, by order, fix, from time to time, such amount as it deems fit:

Provided that different amounts may be fixed for different areas :

Provided further that the amount fixed under this sub-section shall, in no case, be less than twenty-five thousand rupees.

(7) Nothing in this section shall apply to a case where an Inspecting Assistant Commissioner exercises the powers or performs the functions of an income tax Officer in pursuance of an order made u/s 125 or section 125A."

It may also be expedient at this stage to refer to section 143(3) of the Act which deals with the procedure of assessment of income. Sub-section (1) of section 143 empowers the income tax Officer, without requiring the presence of the assessee or production of evidence by him, to make an assessment on the basis of the return. If he is not so satisfied, he is empowered to issue a notice to the assessee under sub-section (2) of section 143 of the Act requiring him to attend his office or produce any evidence to which he may rely in support of his return. If the assessee appears and produces any evidence in support of his return, the income tax Officer, after taking into account all such material or evidence, by an order in writing, shall make the assessment of the total income or loss of the assessee. By the Taxation Laws (Amendment) Act, 1975 section 144 B was inserted in the Act with effect from 1st April, 1976 which provides that where the income tax Officer proposes to make any variation adverse to the assessee in the income or loss returned and the amount of such variation exceeds a sum of Rs. 1,00,000/-, which was the amount fixed by the Board for that purpose, the income tax Officer shall in the first instance forward a draft of the proposed order of assessment to the assessee. On receipt of such a draft order, the assessee" is entitled to file his objections, if any, to such variation within seven days of the receipt of the draft order or within such further period not exceeding fifteen days as the income tax Officer may allow on application made in this behalf. If no such objections are filed within the period of seven days or the extended period, the income tax Officer shall complete the assessment on the basis of the draft order. If any objection is filed by the assessee, he shall forward the objection along with the draft order to the Inspecting Assistant Commissioner and after receiving directions from him shall complete the assessment in terms of the directions which are binding on him. It may be pertinent to recall that section 144B was incorporated in the Act in terms of the recommendations of the Wanchoo Committee in its final report submitted in December, 1971 with the object of giving opportunity to the assessee of meeting with the objections of the income tax Officer before an assessment is finalised. From the scheme and object of section 144B, it is clear that so far as income tax Officer is concerned, the proposed assessment made by him, which is referred to as the "draft assessment order" is final. It is forwarded as a draft order to the assessee only because the variation in the returned income is more than the specified amount i.e. Rs. 1,00,000/- with a view to giving him an opportunity to file objections, if he so desires, and to get suitable directions from the Inspecting Assistant Commissioner. If the assessee does not do so within the specified time of seven days or the time extended by the income tax Officer, the income tax Officer is bound to complete the assessment on the basis of the draft order.

5. It is clear from the expression "the income tax Officer shall complete the assessment on the basis of the draft order" contained in sub-section (3) of

section 144B of the Act that even where objections are received by the income tax Officer, the only function left for him is to forward the objections along with the draft order to the Inspecting Assistant Commissioner and to finalise the assessment in terms of the directions of the Inspecting Assistant Commissioner which are binding on him. Once the draft assessment is prepared and the variation in the returned income being more than Rs. 1,00,000/-, the draft order is forwarded to the assessee as required by section 144B, the quasi judicial function of the income tax Officer comes to end. So far as the income tax Officer is concerned, the draft order is the final assessment order. It is clear from the language of sub-section (3) of section 144B which clearly provides that if no objections are received within the specified period, he shall complete the assessment on the basis of the draft order. That being so, we are of the clear opinion that it is not open to the income tax Officer to forward a second draft order to the assessee after the first draft order is communicated.

6. In the present case, the assessee did not file any objection nor applied for extension of time for the same. It was, therefore, incumbent on the income tax Officer to complete the assessment in terms of the draft order as contemplated by section 144B(3) of the Act. Instead of doing so, he forwarded a second draft order after 10 days of communication of the first draft order enhancing the variation by Rs. 13,76,350/-. This obviously, is beyond the powers conferred on him u/s 143(3) read with section 144B of the Act.

7. We are supported in our above conclusion by the ratio of the decision of the Supreme Court in *Panchamahar Steel Ltd. Vs. U.A. Joshi, ITO and Another*, wherein the Supreme Court has held that the assessee is not entitled to file revised returns after the income tax Officer has made the draft order. It may be pertinent to mention that sub-section (5) of section 139 of the Act provides for submission of revised returns at any time "before the assessment is made". The assessee in that case wanted to submit revised returns after the communication of the draft order. The Supreme Court held that the right to file revised returns under sub-section (5) of section 139 of the Act was to be exercised before making of the draft order in case where section 144B of the Act was applicable. This is so because so far as income tax Officer is concerned, the draft order is the assessment order. Had the variation been not more than Rs. 1,00,000/-, the income tax Officer would not have forwarded a draft order to the assessee. It is because of the variation being in excess of the specified amount of Rs. 1,00,000/- that the income tax Officer was required to forward the same to the assessee as a draft order. It was a draft order only so far as the assessee is concerned. So far as the income tax Officer is concerned, it was final subject only to the directions of the Inspecting Assistant Commissioner, if any, in the event of objections having been filed by the assessee within the specified time.

8. We are also supported in our above conclusion by the decision of the Delhi High Court in *Sudhir Sareen Vs. Income Tax Officer, Central Circle XVII, New Delhi and another*, wherein it was held that if the income tax Officer, acting u/s

144B of the Act, proposes to make any variation to the prejudice of the assessee in the income or loss returned in excess of the limit fixed, he can issue only one draft order of assessment. He has no power under that section to issue more than one draft order. The language of section 144B does not permit any interpretation favouring more than one draft order. It was held that the income tax Officer has no power to issue more than one draft order.

9. We have carefully perused the decision of the Madhya Pradesh High Court in *Banarsidas Bhanot and Sons Vs. Commissioner of Income Tax*, . Calcutta High Court in *Shahdara (Delhi) Saharanpur Light Railway Co. Ltd. (in voluntary liquidation) Vs. Commissioner of Income Tax*, . wherein a contrary view has been taken. We are respectfully in disagreement with the view taken in the above decisions.

10. In view of the above, we answer question No. 1 in the affirmative i.e. in favour of assessee and against the revenue.

11. So far as the second question is concerned, controversy therein pertains to taxability of capital gains. The assessee received compensation amounting to Rs. 85,00,000/- from the insurance company on the destruction of the ship. The cost of the ship was Rs. 55,05,400/-. The income tax Officer included the difference in the income of the assessee as capital gains as, according to him, there was extinguishment of right in a capital asset. The order of the income tax Officer was upheld by the Commissioner of income tax (Appeals) and the income tax Appellate Tribunal. Hence, reference of question No. 2 at the instance of the assessee. The learned counsel for the parties are agreed that the controversy therein now stands concluded by the decision of the Supreme Court in *Vania Silk Mills (P) Ltd. Vs. Commissioner of Income Tax, Ahmedabad [OVERRULED]*, , wherein it has been held that the extinguishment of right in the asset on account of extinguishment of the asset itself is not a transfer of the right in the asset but its destruction. By no stretch of imagination can the destruction of the right on account of the destruction of the asset be equated with the extinguishment of right on account of transfer within the meaning of section 2(47) of the Act. The difference between the amount received by the assessee on the destruction of the asset and the cost thereof, therefore, would not be chargeable to tax u/s 45 of the Act. The learned counsel for the parties are agreed that in view of the above decision, question No. 2 may be answered in favour of the assessee. In view of the above, we answer question No. 2 in the negative i.e. in favour of the assessee and against the revenue.

This reference stands disposed of accordingly with no order as to costs.