

(1969) 02 PAT CK 0008

In the Patna High Court

Case No : Civil Writ Jurisdiction Case No. 34 of 1969

Elphinstone Picture Palace

APPELLANT

Vs

Union of India (UOI) and Another

RESPONDENT

Date of Decision : 26-02-1969

Acts Referred:

Income Tax Act, 1961 — Section 147, 148

Citation : (1969) 74 ITR 115 : (1969) PLJR 299

Hon'ble Judges : Shambhu Prasad Singh, J;S.N.P. Singh, J

Bench : Division Bench

Advocate : Lal Narain Sinha, H.L. Agarwal, G.C. Bharuka and A.S. Sinha, for the Appellant; Tarkeshwar Prasad, Shambhu Sharan and M.N. Verma, for the Respondent

Judgement

Shambhu Prasad Singh, J.—The petitioner, a registered firm, whose main business is exhibition of films, has made this application under Articles 226 and 227 of the Constitution of India for a writ of prohibition restraining the respondents from proceeding against the petitioner on the basis of the notice (annexure " 1 ") u/s 148 of the Income Tax Act, 1961 (hereinafter to be referred as "the Act"), and also for quashing the said notice. The notice was issued to the petitioner by the Income Tax Officer, Ward " A ", Special Circle, Patna, stating that the Income Tax Officer had reason to believe that the petitioner's income chargeable to tax for the assessment year 1961-62 had escaped assessment within the meaning of Section 147 of the Act, and requiring the petitioner, within 30 days from the date of the service of the notice, to file a return in the prescribed form of its income for the said assessment year.

2. Facts relevant for the decision of the case may briefly be stated. The assessment of the petitioner for the assessment year 1960-61 was completed by Shri J. Pathak, the then Income Tax Officer, Special Circle, Patna, accepting the return of the petitioner and the books of account produced. In its return the petitioner had shown that it had taken the following loans :

(i) Loan of Rs. 5,000 on January 12, 1961, through hundi from Seth Mohan Singh Kanhaiyalal, 252/D, Chitranjan Avenue, Calcutta-6--I.T. File No. 522/Md.

(ii) Rs. 10,000 through hundi on February 23, 1961, from Maya Ram Madhav Das Bankers--48, Vivekanand Road, Calcutta-6.--I.T. File No. 346/C/V assessed by Income Tax Officer, Dist. Iltl), Calcutta.

(iii) Rs. 5,000 on January 12, 1961, through hundi from Seth Tirath Das & Sons, 36, Ezra Street, Calcutta-1--I.T. File No. V/1-122-I/IX.

(iv) Rs. 10,000 through hundi on February 23, 1961, from Banshidhar Shyamlal, 48 Vivekanand Road, Calcutta-6--I.T. File No. 131-I/V assessed by I.T.O. Dist. II(1), Calcutta.

According to the respondents, the department was not fully satisfied about the genuineness of these loans and enquiries were being made about it. In the meantime, on the 27th of March, 1967, the Directorate of Inspection, Central Board of Revenue, New Delhi, published a list of bogus hundi brokers and bankers and forwarded copies of it to all the income tax-Officers. The said list contained the names of all the four creditors of the petitioner. On the 15th of October, 1968, the Income Tax Officer issued the impugned notice (annexure " 1 ") to the petitioner.

3. Mr. Lal Narain Sinha, appearing for the petitioner, has contended (i) that the Income Tax Officer who has issued the notice (annexure " 1 ") did not have any material before him for believing that there had been any material non-disclosure by reason of which an under-assessment in the case of the petitioner for the assessment year 1960-61 had taken place and, therefore, he (the Income Tax Officer) had no jurisdiction to issue the said notice, and (ii) that the Income Tax Officer has completely abdicated his jurisdiction to the Directorate of Inspection, Central Board of Revenue, New Delhi; the notice having been issued not on the basis of the belief of the Income Tax Officer but of the Directorate of Inspection is invalid.

4. I propose to take up first for consideration the second point urged by Mr. Sinha. In support of this contention he has placed reliance on the decision in Commissioner of Police, Bombay Vs. Gordhandas Bhanji, . In that case, the Commissioner of Police, Bombay, had communicated to the respondent an order cancelling the permission already granted to the latter for building a cinema house in a part of greater Bombay. On the very face of the communication, the order was of the Government of Bombay and not of the Commissioner who was the appropriate authority to pass such an order. In the circumstances, it was held that the order, not being of the Commissioner, the proper authority, was illegal. It is now well settled that where power is vested to do certain thing in an authority and that authority does not exercise that power itself, but acts according to the dictates of another authority not having such a power without applying itself to the propriety or otherwise of that order, such an order is illegal. It is true that in the instant case too the Income Tax Officer before issuing a notice had himself to

form an opinion that there were reasons for believing that the petitioner had escaped assessment and not the Directorate of Inspection ; but it is nobody's case that the copy of list of bogus hundi brokers and bankers sent by the Directorate of Inspection contained any statement that the petitioner had escaped assessment. It merely provided an information to the Income Tax Officer that four of the creditors of the petitioner were bogus hundi brokers and bankers. On the basis of such information the Income Tax Officer himself has formed an opinion that the petitioner has prima facie escaped assessment. It cannot, therefore, be said that the Income Tax Officer has abdicated his jurisdiction to the Directorate of Inspection. In the notice (annexure " 1 ") there is nothing to indicate that the basis for the notice was not his belief but of somebody else. The question whether the said list can be held a material on the basis of which the Income Tax Officer could form a belief as required by Section 147 of the Act arises for consideration under the first contention of Mr. Sinha and shall be discussed while dealing with that contention. In my opinion, there is no merit in the second contention of Mr. Sinha and it must be rejected.

5. To appreciate the first contention of Mr. Sinha, it is necessary to refer to the relevant provisions of the Act. Section 147 vests the income tax Officer with powers to assess or reassess income chargeable to tax which has escaped assessment for the reasons mentioned therein. This power is subject to the provisions of Sections 148 to 153 and Section 148 lays down that before making the assessment or reassessment a notice must be served on the assessee. Sub-section (2) of Section 148 provides that the Income Tax Officer before issuing any notice under the section shall record his reasons for doing so. Section 149 fixes the period of limitation for issuing a notice u/s 148. As a notice can be issued only if the conditions mentioned in Clauses (a) and (b) of Section 147 are fulfilled, these clauses may be quoted with advantage :

" (a) The Income Tax Officer has reason to believe that by reason of the omission or failure on the part of an assessee to make a return u/s 139 for any assessment year to the Income Tax Officer 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

(b) Notwithstanding that there has been no omission or failure as mentioned in Clause (a) on the part of the assessee, the Income Tax Officer has in consequence of information in his possession reason to believe that income chargeable to tax has escaped assessment for any assessment year."

6. It is conceded by the department that the instant case is not covered by Clause (b) or by the first part of Clause (a). It is covered by the second part of Clause (a). In other words, it is a case where the assessee's income chargeable to tax has escaped assessment by reason of omission or failure on its part to disclose fully and truly all material facts necessary for its assessment. The existence of material for the belief of the Income Tax Officer is justiciable, but its sufficiency or adequacy is not justiciable. In considering the question of the

existence of the material for the belief of the Income Tax Officer the court can also go into the question whether the material is relevant or irrelevant. In cases where the material could not at all be a basis for the belief, the notice has to be struck off. Learned counsel for the parties have relied on a good number of decisions in support of their respective contentions whether the list of the Directorate of Inspection was a relevant or an irrelevant material and whether it could at all be a basis for the belief of the Income Tax Officer that the petitioner's income chargeable to tax had escaped assessment for the year 1960-61. The relevancy or irrelevancy of a material has to be decided with reference to the facts and circumstances of each case. Therefore, the decision cited may not be of much assistance specially when it has been conceded by Mr. Lal Narain Sinha that rules of evidence do not apply to the Income Tax department and what may not be relevant under the Indian Evidence Act may be relevant for formation of a belief of the Income Tax Officer u/s 147 of the Act. Nonetheless, they can throw some light on the question and I now proceed to consider the decisions cited by Mr. Lal Narain Sinha, learned counsel for the petitioner.

7. In Calcutta Discount Company Limited Vs. Income Tax Officer, Companies District, I and Another, the assessee-company in the course of assessment proceedings for the year 1944-45 had represented that the sales of shares in that year were casual transactions and were in the nature of "mere change in investments". It was discovered subsequently that the assessee was in fact carrying on business of selling shares contrary to its earlier representations and in the assessment for the years 1945-46 and 1946-47 profits earned by sale of shares were included in the total assessable income of the company and that by its memorandum and articles of association, the company was authorised to carry on business of diverse kinds specially to hold and deal in shares and securities and to carry on business as financiers. According to the Income Tax Officer, these were the basis for his belief that the company had been under-assessed. Majority of the judges of the Supreme Court held that, in the circumstances of the case, the Income Tax Officer who issued the notices did not have any material before him for believing that there had been any material non-disclosure by reason of which an under-assessment had taken place. Really they held that it was not a case of non-disclosure of any material facts by the assessee, inasmuch as full details as regards sales of shares had in fact been disclosed, and the company was not required by law to state what was its true intention behind the sale of shares and that was an inferential fact, the inference to be drawn by the assessing authority from the material facts taken in conjunction with the surrounding circumstances.

8. In Commissioner of Income Tax, Gujarat Vs. A. Raman and Company, the assessee was a firm composed of managers of two Hindu undivided families. After the original assessments were made on the assessee for the assessment years 1959-60, 1960-61 and 1961-62, the Income Tax Officer issued notice u/s 147(b) of the Act to reopen the assessments. The alleged material for the belief

of the Income Tax Officer was that he had received information that the assessee had effected sales of goods to the families and that those families had earned substantial profits on the re-sale of those goods over and above the margin of profits earned by the assessee and that the creation of the family business was merely a subterfuge or a contrivance of the partners of the assessee to divert the profits. The Supreme Court upheld the striking off of the notice and observed :

"But the law does not oblige a trader to make the maximum profit that he can out of his trading transactions. Income which accrues to a trader is taxable in his hands : income which he could have, but has not earned, is not made taxable as income accrued to him. By adopting a device, if it is made to appear that income which belonged to the assessee had been earned by some other person, that income may be brought to tax in the hands of the assessee, and if the income has escaped tax in a previous assessment a case for commencing a proceeding for reassessment u/s 147(b) may be made out. Avoidance of tax liability by so arranging commercial affairs that charge of tax is distributed is not prohibited. A taxpayer may resort to a device to divert the income before it accrues or arises to him. Effectiveness of the device depends not upon considerations of morality, but on the operation of the Income Tax Act. Legislative injunction in taxing statutes may not, except on peril of penalty, be violated, but it may lawfully be circumvented. "

9. It was further observed that it was not the case of the department that the income which had escaped assessment was in fact earned by the assessee.

10. *Ramniwas Kanailal Vs. S.P. Shende*, Income Tax Officer, D-1 Ward, Bombay, was a case where the sole ground for issuing notices u/s 34(1)(a) of the old Act was the failure of the assessee to disclose an account claimed by him to be outstandings of a business which had been wound up. The records of the case showed that the Income Tax Officer had no personal knowledge of the proceedings of the assessment years in respect of which the notices of reassessment were issued and most of the records pertaining to the assessment of the assessee for previous years were lost. In the circumstances, the learned judges of the Bombay High Court held that there was no basis for the belief of the Income Tax Officer that the account represented acquisitions made by the assessee for the years for which the reassessment was sought to be made. In the opinion of the learned judges, there was also no proof of omission or failure on the part of the assessee to disclose fully or truly the material facts necessary for his assessments for the years 1940-41 to 1945-46. It may be stated here that Section 34 of the old Act has been re-enacted as Section 147 in the new Act.

11. Of the cases discussed above, *Ramniwas Kanailal*'s case is a case where there was no material at all for the basis of the belief of the Income Tax Officer and in the other two cases, the assessee under the law was not bound to disclose materials which, in the opinion of the Income Tax officials, amounted to omission or failure to disclose material facts. In the instant case, if the loans mentioned in the petitioner's return for the assessment year 1960-61 were bogus and really

not advanced to it, there can be no doubt that it did not disclose truly the material facts in its return. But Mr. Lal Narain Sinha has contended that whether the creditors of the petitioner were bogus hundi brokers and bankers, as mentioned in the list of the Directorate of Inspection, was not at all a relevant fact for the purpose of forming an opinion as to whether the petitioner had omitted or failed to disclose truly material facts. What was relevant was whether in fact the loans were advanced to the petitioner or not, because even bogus hundi brokers and bankers sometimes may really advance loans. According to Mr. Sinha, therefore, the list of the Directorate of Inspection could not be the basis of the belief of the Income Tax Officer as required by Section 147 of the Act for issuing a notice against the petitioner in the instant case. In support of this contention he has relied on an unreported decision of the Supreme Court in Civil Appeals Nos. 2274 to 2276 of 1966 : Rohtas Industries Ltd. v. S. D. Agarwal, [1969] 39 Comp. Cas. 781 (S.C.) (judgment dated the 16th December, 1968). In that case the Central Government appointed an inspector to investigate the affairs of the Rohtas Industries Ltd. u/s 237(b) of the Companies Act, 1956. The relevant portions of Section 237 of the Companies Act run as follows :

" Without prejudice to its powers u/s 235, the Central Government.....

(b) may do so if, in the opinion of the Central Government, there are circumstances suggesting--

(i) that the business of the company is being conducted with intent to defraud its creditors, members, or any other persons, or otherwise for a fraudulent or unlawful purpose, or in a manner oppressive of any of its members, or that the company was formed for any fraudulent or unlawful purpose ;

(ii) that persons concerned in the formation of the company or the management of its affairs have in connection therewith been guilty of fraud, misfeasance or other misconduct towards the company or towards any of its members; or

(iii) that the members of the company have not been given all the information with respect to its affairs which they might reasonably expect, including information relating to the calculation of the commission payable to a managing or other director, the managing agent, the secretaries and treasurers, or the manager of the company. "

12. It was, stated in the order appointing the inspector in the case of Rohtas Industries Ltd. that the said company was being conducted with intent to defraud its creditors, members or other persons and the persons concerned in the management of its affairs had in connection therewith been guilty of fraud, misfeasance, or other misconduct towards the said company or its members. This order was challenged by an application under Article 226 of the Constitution of India before this court which dismissed the same. There was an appeal to the Supreme Court which was allowed. According to the affidavit filed by the then Secretary to the Government of India, Ministry of Finance, Department of Company Affairs and Insurance, and Chairman, Company Law Board, before this

court. S. P. Jain together with his friends, relations and associates was principally in charge of the management of the Rohtas Industries Ltd. and S. P. Jain had been found previously guilty of misconduct, etc., in the management of other companies run by him. This was the main basis for the opinion of the Central Government that there were circumstances suggesting fraud, etc., by the management of the Rohtas Industries Ltd. towards the company or its members. The Supreme Court held that as the Central Government in appointing an inspector for investigation appeared to have been oppressed by their opinion about S. P. Jain, the order was illegal. It was further observed in the judgment that, though the formation of the opinion by the Central Government was subjective, the existence of the circumstances relevant to the inference as the sine qua non for action must be demonstrable ; if their existence was questioned, it had to be proved at least prima facie. According to Mr. Sinha, the Income Tax Officer for forming the belief u/s 147 of the Act must act objectively and the test laid down by the Supreme Court in Rohtas Industries case for the matter of subjective formation of the opinion must apply with greater rigour in the matter of formation of belief u/s 147 of the Act. There can be no doubt that the test laid down by the Supreme Court in the matter of formation of opinion u/s 237 of the Companies Act ought to apply in the matter of formation of belief u/s 147 of the Act. What must be demonstrable and has to be proved prima facie is not the inference, but the existence of the circumstance relevant to the inference and that circumstance in the instant case is that the creditors are bogus hundi brokers and bankers, the existence of which is proved prima facie by the list of the Directorate of Inspection. Merely because, in the circumstances of that case, the Supreme Court held that the conduct of S. P. Jain with regard to the management of his other concerns was not relevant in the matter of formation of an opinion as to fraud, etc., by the management of Rohtas Industries Ltd., it cannot be said that in the instant case the fact that the alleged creditors of the petitioner are bogus hundi brokers and bankers is also irrelevant for formation of the belief by the Income Tax Officer. In my opinion, the decisions relied on by Mr. Sinha do not help the petitioner on the facts and in the circumstances of this case. On the other hand, learned counsel for the respondents has relied on the following decisions :

(i) West India Cotton Association Ltd. Vs. V.K. C. Rao, Income Tax Officer, Companies Ward, Ahmedabad, . In this case the report of the inspector was considered sufficient information justifying action u/s 147 of the Act by Justice Shelat of the Gujarat High Court (as he then was).

(ii) Sowdagar Ahmed Khan (Deceased) (By his Legal representatives) Vs. Income Tax Officer, Nellore, . According to this decision, even where there was some material before the Income Tax Officer on which he formed a prima facie belief that the assessee had omitted to disclose fully and truly all material facts and that in consequence of such non-disclosure income had escaped assessment, the Income Tax Officer had jurisdiction to issue notices u/s 34 of the old Act. Of course, the facts of that case were quite different from the facts before us. There

the assessee had failed to disclose the existence of a bank account in the name of his father-in-law which was benami for the benefit of the assessee and was in the habit of introducing money and holding properties in benami names. Facts of two cases can never be similar, but the use of the word "some" before "material" by the Supreme Court in the observation referred to above is pertinent.

(iii) S. Narayanappa and Others Vs. Commissioner of Income Tax, Bangalore, . In this case it was re-emphasised that whether the grounds for the belief of the Income Tax Officer u/s 34 of the old Act are adequate or not is not a matter for the court to investigate, that is, the sufficiency of the grounds which induced the Income Tax Officer to act is not a justiciable issue.

13. In my opinion, the list of the Directorate of Inspection was not irrelevant for the purpose of formation of the belief by the Income Tax Officer u/s 147 of the Act, and the question whether it is sufficient or adequate for the belief, cannot be gone into.

14. For the foregoing reasons, I find no merit in this application and it is accordingly dismissed with costs. Hearing fee is assessed at Rs. 250.

S.N.P. Singh, J.

15. I agree.