

(2010) 10 DEL CK 0003

In the Delhi High Court

Case No : Writ Petition (C) No. 6087 of 2010

Sarthak Securities Co. Pvt. Ltd.

APPELLANT

Vs

Income Tax Officer

RESPONDENT

Date of Decision : 18-10-2010

Acts Referred:

Constitution of India, 1950 — Article 226

Income Tax Act, 1961 — Section 139, 142(1), 143(1), 143(3), 147

Citation : (2011) 1 AD 226 : (2010) 236 CTR 362 : (2010) 174 DLT 161 :
(2010) 329 ITR 110 : (2010) 195 TAXMAN 262

Hon'ble Judges : Dipak Misra, C.J.; Manmohan, J

Bench : Division Bench

Advocate : Udaibir Singh Kochar, for the Appellant; Rashmi Chopra, for the Respondent

Judgement

Dipak Misra, C.J.—By this writ preferred under Article 226 of the Constitution of India, the assessee-petitioner has prayed for issue of a writ of certiorari for quashment of the notice dated 25th March, 2010, Annexure P-II, issued u/s 148 of the Income Tax Act, 1961 (for brevity "the Act") pertaining to the assessment year 2003-04 by the Income Tax Officer, the 1st respondent herein.

2. The facts which are imperative to be unfurled are that the assessee-petitioner filed its return for the assessment year 2003-04 on 31st March, 2004 declaring an income of Rs. 15,360/-. The said return was processed and intimation u/s 143(1) was issued on 6th April, 2004 accepting the return. As put forth, the petitioner decided to issue shares in accordance with its Memorandum and Articles of Association during the previous year relevant to the assessment year 2003-04 and for the said purpose approached a number of prospective investors. Four private limited companies, namely, Nishant Finvest Pvt. Ltd., Shri Dinanath Luhhariwal Spinning Mills Pvt. Ltd., Division Trading Pvt. Ltd and K.R. Fincap Pvt. Ltd., decided to invest in the shares of the petitioner company. As pleaded, after observing all the legal formalities, the assessee-petitioner allotted the shares to these four companies on 31st March, 2003. The amount invested by the said

companies are Rs. 2,50,000/-, Rs. 2,50,000/-, Rs. 3,00,000/- and Rs. 2,50,000/- respectively. The above-named companies were active as per the records of the Registrar of Companies (ROC) and are assessed to Income Tax and have been allotted permanent account numbers by the Income Tax Department.

3. As pleaded, on 25th March, 2010, a notice u/s 148 of the Act was issued by the respondent No. 1 to the petitioner alleging that he had reason to believe that the income chargeable to tax for the assessment year 2003-04 had escaped assessment within the meaning of Section 147 of the Act and, accordingly, he required the petitioner to file the return for the said assessment year. In response to the said notice, the assessee-petitioner requested vide letter dated 28th April, 2010 to treat the return of income filed on 31st March, 2004 to be the return which would deem to have been filed in compliance with the notice. The assessee-petitioner also requested the respondent to provide a copy of the reasons recorded u/s 148(2) and the approval for issuance of notice. The respondent furnished the reasons recorded by him vide letter dated 21st July, 2010. While furnishing the reasons, the respondent also initiated assessment proceedings by issuing formal notices. The assessee through his authorized representative raised objections to the initiation of the proceedings u/s 147 of the Act on the foundation that the same had not been initiated in accordance with law. Be it noted, in the objections, many a ground was raised and reliance was placed on the decision rendered by the Apex Court in CIT v. Lovely Exports (P) Ltd. 216 CTR 195 (SC) and on the decision of this Court in CIT v. SFIL Stock Broking Ltd. ITA No. 1056/2009.

4. The respondent No. 1, by order dated 25th August, 2010, rejected the objections raised by the petitioner and issued notices for fixing the hearing to 27th August, 2010.

5. Be it noted, the matter was finally heard with the consent of the learned Counsel for the parties. We have heard Mr. Udaibir Singh Kochar, learned Counsel for the assessee-petitioner, and Ms. Rashmi Chopra, learned Counsel for the revenue.

6. It is contended by Mr. Kochar that the reasons recorded for initiation of proceedings u/s 147(2) do not disclose the basis. The proceedings have been initiated on the ground of information received from the investigation wing but the order of the assessing officer does not reflect any independent application of mind to the information so received. It is urged that the respondent No. 1 has failed to appreciate the ratio laid down in the decision rendered in Lovely Exports (P) Ltd. BI (supra) when all the requisite information was available with the assessing officer from the very beginning.

7. Ms. Rashmi Chopra, learned Counsel for the revenue, in support of the order, submitted that the order passed by the assessing officer reflects application of mind and the sufficiency of reasons cannot be gone into at this stage.

8. The singular question that emerges for consideration is whether in the case at

hand, the initiation of proceedings u/s 147 is justified in law or not.

9. The assessing officer, while issuing the notice, has stated thus:

Whereas I have reason to believe that your income chargeable to tax for the assessment year 2003-2004 has escaped assessment within the meaning of Section 147 of the Income Tax Act, 1961.

I, therefore, propose to assess/reassess the income for the said assessment year and I hereby require you to deliver to me within 20 days from the date of service of this notice, a return in the prescribed form of the income of your income in respect of which you are assessable for the said assessment year.

10. After receipt of the said notice, the petitioner submitted that the return of income, as filed earlier, should be treated as the return in compliance with the notice under reference. In the said letter, he asked for reasons to enable him to file the objections. After receipt of the said letter, the respondent No. 1, the assessing officer, sent a communication vide Annexure-XI wherein it has been stated thus:

M/s Sarthak Securities P Ltd

AY 2003-04

19/3/2010 Information was received from the office of the Addl DIT (Investigation) Unit-V. that M/s Sarthak Securities P Ltd had received bogus accommodation entries during the FY 2002-03 relevant to the AY 2003-04 as per details placed contra.

Beneficiary Name

Beneficiary Bank

Beneficiary Branch

Value of Entry

Instrument No. by which entry taken

Date on which entry taken

Name of A/c holder of entry giving a/c

Bank from which entry given

Branch of entry giving bank

Sarthak Securities P. Ltd.

OBC

Saket

2500000/-

17/12/02

Nishant Finvest

SBBJ

NRR

Do

Do

Do

2500000/-

18/9/ 02

Dinanath Luhhari Wal Spinning Mill

SBP

DG

DO

DO

DO

2500000/-

16/12/02

K.R. Fincap P Ltd

SBBJ

NRR

DO

DO

DO

300000/-

12/3/ 03

Division Trading P Ltd.

BOR

Rohtak Rd.

According to the information received from the DIT (Inv) the accommodation entries are received as share application money or as unsecured loan. The

assessee's Balance sheet as on 31/3/2003 showed that there is introduction of share capital of Rs. 284800/- and share premium of Rs. 865000/-.

In this case return of income for the AY 2003-04 was filed on declaring income of Rs. 15360/- and as per records asstt has not been completed u/s 143(3) of the I.T. Act.

As the assessee had received bogus accommodation entry of Rs. 1050000/- during the AY 2003-04, I have reason to believe that income chargeable to tax has escaped assessment.

11. After receipt of the said communication, the assessee-petitioner filed objections to the initiation of proceedings u/s 147 of the Act. We think it apposite to reproduce the main part of the objections, which read as follows:

1. The reasons do not disclose the basis on which the Addl. DIT has termed the receipt of money by the assessee from four incorporated bodies viz. Nishant Finvest (P) Ltd., Shri Dinanath Luhariwala Spining Mills (P) Ltd., K.R. Fincap (P) Ltd. and Division Trading (P) Ltd. towards share application money as bogus accommodation entries. If any investigations were carried out by Addl. DIT or any witnesses were examined by him who implicated the assessee, the report of such investigations or the statements of the witnesses do not form part of the reasons

2. "..."

3. Further, the alleged information provided by the Addl. DIT has been accepted as gospel truth without any verification by the A.O. The law postulates the A.O. (and not the Addl. DIT) to have reason to believe. Blind acceptance of the information furnished by the Addl. DIT cannot form reasons leading to the belief by the A.O. of any escapement of income.

4. The A.O. has to independently apply his mind to the information received from the Addl. DIT and arrive at the belief that income has escaped assessment....

In the instant case, the reasons recorded do not show any application of mind nor the same show any belief independently arrived at, which is the basic pre requisite for issuing notice u/s 148.

5. At any rate, the alleged bogus shareholders are all incorporated and active companies as per the records of Registrar of Companies. Moreover, as per the alleged information provided by the Addl. DIT himself, all of them had bank accounts and payments were made by them to the assessee company through banking channels. As such the identity of the shareholders stands duly accepted even by the Addl. DIT on whose information the proceedings have been initiated....

6. In the instant case, the names of the shareholders have been provided by the Addl. DIT himself and are also incorporated in the reasons recorded u/s 148. Hence, in case the department feels that they were accommodation entry

providers, it is free to proceed against them.

12. The said objections have been rejected on 25th August, 2010, mainly stating, inter alia, as follows:

In this regard, I hereby bring to your notice that, further to the information received from the Investigation Wing and on subsequent detailed examination, inter alia, of Bank statements on record, I have strong reasons to form this honest and reasonable belief that you have, during the financial year 2002-03, transacted with:

- a) M/s Nishant Finvest on 17-12-2002 for an amount of Rs. 2,50,2000/-.
- b) M/s Dinanath Luhhariwal Spinning Mill on 18-09-2002 for an amount of Rs. 2,50,000/-
- c) M/s K.R. Fincap Pvt Ltd on 16-12-2002 for an amount of Rs. 2,50,000/- and
- d) M/s Division Trading Pvt Ltd on 12-3-2003 for an amount of Rs. 3,00,000/-

And have used the aforesaid entities as a conduit to absorb your own unaccounted monies and as such have accommodated with these entities.

After so stating, the assessing officer distinguished the decisions relied on by the assessee and rejected the objections.

13. It is submitted by Mr. Singh, learned Counsel for the petitioner, that there has been no application of mind and further no new material has been brought to his notice. It is contended by him that the assessing officer was very much aware of the names of the existing four companies and that being the position, the decision in Lovely Exports P. Ltd. (supra) gets squarely attracted and not following the ratio of the said decision amounts to improper exercise of power which makes the order vulnerable and totally untenable.

14. In this context, we think it apt to refer to Section 147 of the Act, which reads as under.

147. Income escaping assessment. If the Assessing Officer 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 to 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 this section, or recompute the loss or the depreciation allowance or any other allowance, as the case may be, for the assessment year concerned (hereafter in this section and in Sections 148 to 153 referred to as the relevant assessment year):

Provided that where an assessment under Sub-section (3) of Section 143 or this section has been made for the relevant assessment year, no action shall be taken under this section after the expiry of four years from the end of the relevant assessment year, unless any income chargeable to tax has escaped assessment

for such assessment year by reason of the failure on the part of the assessee to make a return u/s 139 or in response to a notice issued under Sub-section (1) of Section 142 or Section 148 or to disclose fully and truly all material facts necessary for his assessment for that assessment year:

Provided further that the Assessing Officer may assess or reassess such income, other than the income involving matters which are the subject-matters of any appeal, reference or revision, which is chargeable to tax and has escaped assessment. Explanation 1.-Production before the Assessing Officer of account books or other evidence from which material evidence could, with due diligence, have been discovered by the Assessing Officer will not necessarily amount to disclosure within the meaning of the foregoing proviso.

Explanation 2.-For the purposes of this section, the following shall also be deemed to be cases where income chargeable to tax has escaped assessment, namely:-

(a) where no return of income has been furnished by the assessee although his total income or the total income of any other person in respect of which he is assessable under this Act during the previous year exceeded the maximum amount which is not chargeable to Income Tax;

(b) where a return of income has been furnished by the assessee but no assessment has been made and it is noticed by the Assessing Officer that the assessee has understated the income or has claimed excessive loss, deduction, allowance or relief in the return;

(c) where an assessment has been made, but-

(i) income chargeable to tax has been under assessed ; or

(ii) such income has been assessed at too low a rate; or

(iii) such income has been made the subject of excessive relief under this Act; or

(iv) excessive loss or depreciation allowance or any other allowance under this Act has been computed.

Explanation 3.-For the purpose of assessment or reassessment under this section, the Assessing Officer may assess or reassess the income in respect of any issue, which has escaped assessment, and such issue comes to his notice subsequently in the course of the proceedings under this section, notwithstanding that the reasons for such issue have not been included in the reasons recorded under Sub-section (2) of Section 148.

15. On scanning of the anatomy of the aforesaid provision, it is clear as crystal that the formation of belief is a condition precedent as regards the escapement of the tax pertaining to the assessment year by the assessing officer. The assessing officer is required to form an opinion before he proceeds to issue a notice. The validity of reasons, which are supposed to sustain the formation of an

opinion, is challengeable. The reasons to believe are required to be recorded by the assessing officer.

16. In this regard, it is apt to reproduce a passage from N.D. Bhatt, Inspecting Assistant Commissioner and Another Vs. I.B.M. World Trade Corporation.,

It is also well-settled that the reasons for reopening are required to be recorded by the assessing authority before issuing any notice u/s 148 by virtue of the provisions of Section 148(2) at the relevant time. Only the reason so recorded can be looked at for sustaining or setting aside a notice issued u/s 148. In the case of *EQUITABLE INVESTMENT CO. (P.) LTD. Vs. Income Tax OFFICER, G. WARD, AND OTHERS.*, a Division Bench of the Calcutta High Court has held that where a notice issued u/s 148 of the Income Tax Act, 1961, after obtaining the sanction of the Commissioner of Income Tax is challenged, the only document to be looked into for determining the validity of the notice is the report on the basis of which the sanction of the Commissioner of Income Tax has been obtained. The Income Tax Department cannot rely on any other material apart from the report.

17. In *Hindustan Lever Ltd. Vs. R.B. Wadkar*, Assistant Commissioner of Income Tax and Others (No. 1), a Division Bench has opined thus:

...the reasons are required to be read as they were recorded by the Assessing Officer. 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 Assessing Officer to disclose and open his mind through reasons recorded by him. He has to speak through his reasons. It is for the Assessing Officer to reach to 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 Assessing Officer 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. Reasons are the manifestation of mind of the Assessing Officer. 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 Assessing Officer, 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. The reasons recorded by the Assessing Officer cannot be supplemented by filing an affidavit or making an oral submission, otherwise, the reasons which were lacking in the material particulars would get supplemented, by the time the matter reaches to the court, on the strength of affidavit or oral submissions advanced.

[underlining is ours]

18. In Assistant Commissioner of Income Tax Vs. Rajesh Jhaveri Stock Brokers Pvt. Ltd., it has been ruled thus:

Section 147 authorises and permits the Assessing Officer 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 Assessing Officer 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 Assessing Officer should have finally ascertained the fact by legal evidence or conclusion. The function of the Assessing Officer is to administer the statute with solicitude for the public exchequer with an inbuilt idea of fairness to taxpayers. As observed by the Supreme Court in Central Provinces Manganese Ore Co. Ltd. Vs. I.-T.O., Nagpur, for initiation of action u/s 147(a) (as the provision stood at the relevant time) fulfillment of the two requisite conditions in that regard is essential. At that stage, the final outcome of the proceeding is not relevant. In other words, at the initiation stage, what is required is "reason to believe", but not the established fact of escapement of income. At the stage of issue of notice, the only question is whether there was relevant material on which a reasonable person could have formed a requisite belief. Whether the materials would conclusively prove the escapement is not the concern at that stage. This is so because the formation of belief by the Assessing Officer is within the realm of subjective satisfaction.

[Emphasis supplied]

19. In this context, we may refer with profit to a Division Bench decision of this Court in ITA No. 1056/2009 The Commissioner of Income Tax III v. SFIL Stock Broking Ltd. decided on 27th April, 2010 wherein the Bench was dealing with the validity of the proceedings u/s 147 of the Act. The Bench reproduced the initial issuance of notice and thereafter referred to the reasons for issue of notice u/s 148 which was provided to the assessee. Thereafter, the Bench referred to the decisions in The Commissioner of Income Tax Vs. Shri Atul Jain, Jay Bharat Maruti Ltd. v. CIT 223 CTR 269 (Del) and CIT v. Batra Bhatta Company 174 Taxman 444 (Del) and eventually held thus:

9. In the present case, we find that the first sentence of the so-called reasons recorded by the Assessing Officer is mere information received from the Deputy Director of Income Tax (Investigation). The second sentence is a direction given by the very same Deputy Director of Income Tax (Investigation) to issue a notice u/s 148 and the third sentence again comprises of a direction given by the Additional Commissioner of Income Tax to initiate proceedings u/s 148 in respect of cases pertaining to the relevant ward. These three sentence are followed by the following sentence, which is the concluding portion of the so-called reasons:

Thus, I have sufficient information in my possession to issue notice u/s 148 in

the case of M/s SFIL Stock Broking Ltd. on the basis of reasons recorded as above.

10. From the above, it is clear that the Assessing Officer referred to the information and the two directions as "reasons" on the basis of which he was proceeding to issue notice u/s 148. We are afraid that these cannot be the reasons for proceeding u/s 147/148 of the said Act. The first part is only an information and the second and the third parts of the beginning paragraph of the so-called reasons are mere directions. From the so-called reasons, it is not at all discernible as to whether the Assessing Officer had applied his mind to the information and independently arrived at a belief that, on the basis of the material which he had before him, income had escaped assessment. Consequently, we find that the Tribunal has arrived at the correct conclusion on facts. The law is well settled. There is no substantial question of law which arises for our consideration.

[Emphasis is ours]

20. On a perusal of the aforesaid decisions, it is graphically clear that once the ingredients of Section 147 are fulfilled, the assessing officer is competent in law to initiate the proceedings u/s 147. To put it differently, the conditions precedent as engrafted in the said provision are to be satisfied.

21. At this juncture, it is profitable to refer to the authority in GNK Driveshafts (India) Ltd. v. Income Tax Officer and Ors. (2003) 179 C54 (SC) 11 wherein their Lordships of the Apex Court have held thus:

5. We see no justifiable reason to interfere with the order under challenge. However, we clarify that when a notice u/s 148 of the Income Tax Act is issued, the proper course of action for the notice is to file return and if he so desires, to seek reasons for issuing notices. The assessing officer is bound to furnish reasons within a reasonable time. On receipt of reasons, the notice is entitled to file objections to issuance of notice and the assessing officer is bound to dispose of the same by passing a speaking order. In the instant case, as the reasons have been disclosed in these proceedings, the assessing officer has to dispose of the objections, if filed, by passing a speaking order, before proceeding with the assessment in respect of the abovesaid five assessment years.

22. In *Lovely Exports (P) Ltd.* (supra), the Apex Court held thus:

2. Can the amount of share money be regarded as undisclosed income u/s 68 of Income Tax Act, 1961? We find no merit in this SLP for the simple reason that if the share application money is received by the assessee company from alleged bogus shareholders, whose names are given to the assessing officer, then the department is free to proceed to reopen their individual assessments in accordance with law. Hence, we find no infirmity with the impugned judgment.

23. The obtaining factual matrix has to be tested on the anvil of the aforesaid pronouncement of law. In the case at hand, as is evincible, the assessing officer

was aware of the existence of four companies with whom the assessee had entered into transaction. Both the orders clearly exposit that the assessing officer was made aware of the situation by the investigation wing and there is no mention that these companies are fictitious companies. Neither the reasons in the initial notice nor the communication providing reasons remotely indicate independent application of mind. True it is, at that stage, it is not necessary to have the established fact of escapement of income but what is necessary is that there is relevant material on which a reasonable person could have formed the requisite belief. To elaborate, the conclusive proof is not germane at this stage but the formation of belief must be on the base or foundation or platform of prudence which a reasonable person is required to apply. As is manifest from the perusal of the supply of reasons and the order of rejection of objections, the names of the companies were available with the authority. Their existence is not disputed. What is mentioned is that these companies were used as conduits. In that view of the matter, the principle laid down in *Lovely Exports (P) Ltd.* (supra) gets squarely attracted. The same has not been referred to while passing the order of rejection. The assessee in his objections had clearly stated that the companies had bank accounts and payments were made to the assessee company through banking channel. The identity of the companies was not disputed. Under these circumstances, it would not be appropriate to require the assessee to go through the entire gamut of proceedings. It is totally unwarranted.

24. Resultantly, the initiation of proceedings u/s 147 and issuance of notice u/s 148 of the Act are hereby quashed. In the facts and circumstances of the case, there shall be no order as to costs.