

A.O CANNOT ISSUE NOTICE U/S 148 ON THE BASIS OF SCANTY AND VAGUE INFORMATION AND MATERIAL WHICH DO NOT INDICATE ESCAPEMENT OF INCOME

Signature Hotels (P) Ltd Vs ITO (Delhi HC) - When the reason recorded for initiation of reassessment proceedings and the information received is extremely scanty and vague, and the material based on which the proceedings are initiated does not indicate escapement of income, the AO will have no jurisdiction to issue notice u/s 148.

Signature Hotels (P) Ltd. Vs. ITO

Delhi High Court

Writ Petition (Civil) No. 8067/2010

Date of order: 21st July, 2011

Judgment

SANJIV KHANNA, J.:

The petitioner is a company, which was incorporated on 30th September, 2002 and for the first year, i.e., the assessment year 2003-04, had filed its return of income on 31st March, 2005. The return was not selected for scrutiny. Subsequently, the Assessing Officer issued two notices dated 22nd March, 2010 and 29th March, 2010 under Section 148 of the Income-Tax Act, 1961 (Act, for short) for assessment. The petitioner has impugned these two notices on the ground that the pre-conditions for issue of notice under Section 148 are not satisfied and, therefore, the Assessing Officer is exceeding his jurisdiction. The petitioner has also impugned the order dated 15th November, 2010 passed by the Income-Tax Officer, Ward 8(4), New Delhi rejecting their objections to initiation of proceedings under Section 148 of the Act. The said order was passed as the assessee had filed objections to the initiation of proceedings under Section 148 and in terms of the decision of the Supreme Court in GKN Driveshafts (India) Limited versus Income Tax Officer and Others, [2003] 259 ITR 19 (SC).

2. The question, which arises for consideration, is whether the proceedings initiated under Section 147/148 of the Act are invalid for want of jurisdiction as the pre-conditions for initiation of the said proceedings as stipulated in Section 147 of the Act are not satisfied.

3. Section 147 of the Act reads as under:

“Section 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 under section 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.

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 underassessed; 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.”

4. The aforesaid Section is wide but it is not plenary. We have to consider and examine the crucial expression “reason to believe” used in the said Section. The Assessing Officer must have “reason to believe” that an income chargeable to tax has escaped assessment. This is mandatory and the “reasons to believe” are required to be recorded in writing by the Assessing Officer. Sufficiency of reasons is not a matter, which is to be decided by the writ court, but existence of

belief is the subject matter of the scrutiny. A notice under Section 148 can be quashed if the “belief” is not bona fide, or one based on vague, irrelevant and non-specific information. The basis of the belief should be discernible from the material on record, which was available with the Assessing Officer, when he recorded the reason. There should be a link between the reasons and the evidence/material available with the Assessing Officer. However, as we are dealing with initiation of proceedings, it is not necessary that the material should conclusively prove the escapement. The “reasons to believe” would mean cause or justification of the Assessing Officer to believe that the income has escaped assessment and do not mean that the Assessing Officer should have finally ascertained the said fact by legal evidence or reached a conclusion, as this is determined and decided in the assessment order, which is the final stage before the Assessing Officer.

5. Before dealing with the facts of the case, we may notice some judgments of the Supreme Court when proceedings under Section 147/148 of the Act can be initiated on statements made by third person on the account of “accommodation entry”. In ITO versus Lakhmani Mewal Das, [1976] 103 ITR 437 (SC), the Supreme Court affirmed the decision of the High Court and held that there was nothing to show in the confession made by a third party related to the loan taken by the assessee much less a loan which was shown to have advanced by that person to the assessee and, therefore, live link or close nexus, which should be there between the material and the belief formed by the Assessing Officer was missing or was too tenuous to provide legal sound basis for initiation of assessment proceedings under Section 147. After referring to this judgment, a Division Bench of Delhi High Court, in Income-Tax Officer, Special Civil No. VII, New Delhi, and Another versus Dwarka Dass and Brothers, [1981] 131 ITR 571 (Del) has held as under:

“...The Supreme Court, affirming the decision of the High Court, held that there was nothing to show that the confession of M.K. related to a loan to the assessee, much less to the loan which was shown to have been advanced by that person to the respondent and the live link or close nexus which should be there between the material before the ITO and the belief which he was to form was missing or was, in any event, too tenuous to provide a legally sound basis for reopening the assessment....

The position in the present case falls within the same category. At the time of the original assessment all the facts relating to the cash credits in question were fully disclosed. This has been found by the learned Judge at page 960 (of 118 ITR) and indeed this is the accepted position on the basis of which even the proposal of the ITO to the Commissioner (set out at page 964) proceeded. Thereafter, the only material received by the ITO appears to be that the revenue authorities had carried out certain investigations, that they had discovered the existence of bogus hundi brokers who were allegedly lending their names to assessee and that a list had been circulated to various ITOs of the hundi brokers who were allegedly indulging in malpractices. The internal audit party appears to have discovered that some of the creditors whose credits had been accepted in the assessee’s case fell within this category and raised an audit objection which

was the immediate provocation for the reopening of the assessment. In this case also, as in the case before the Supreme Court, there is no live connection or link established between the information or the facts, in the possession of the ITO, and the genuineness of the particular loans recorded in the assessee's books. The mere fact that the names of the some of the creditors figured in a list made out by the department would be too general and vague to lead to an inference regarding the truth or otherwise of the loans recorded by the assessee. We are wholly unable to find any material point of distinction between the facts of the present case and those considered by the Supreme Court in the case of Lakhmani Mewal Das [1976] 103 ITR 437.”

6. The view taken by the Supreme Court in Lakhmani Mewal Das (supra) was followed in Ganga Saran and Sons Private Limited versus Income-Tax Officer-I, [1981] 130 ITR 1 (SC). The matter was again examined by the Supreme Court in Phool Chand Bajrang Lal and Another versus Income-Tax Officer and Another, [1993] (203) ITR 456 (SC). In the said case, information was received by the Assessing Officer that the third company had never actually advanced loans to any person and the said third company was in the business consisting entirely of name lending. Noticing the judgment in Lakhmani Mewal Das (supra) it was held that the nature of information which was available was vastly different. In the case of Lakhmani Mewal Das (supra), the information was extremely vague and scanty whereas in the case of Phool Chand Bajrang Lal (supra), the information was specific, unambiguous and clear.

7. In the present case the undated reasons recorded by the Assessing Officer for initiation of proceedings read as under:

” Information received from the office of the DIT (Inv.)-VI, New Delhi revealed that M/s Signature Hotels (P) Ltd. has introduced unaccounted money in its books of account during F.Y. 2002-03 through accommodation entry from M/s Swetu Stone PV for Rs.5.00 lac.

In view of the above, I have reasons to believe that taxable income to the tune of Rs.5.00 lac has escaped assessment within the meaning of section 147 of the I.T. Act, 1961.”

8. However, the aforesaid reasons are not the same/identical when we compare the reasons recorded by the Assessing Officer in the approval proforma for initiation of action under Section 147/148. The reasons recorded by the Assessing Officer for approval of the Commissioner of Income-Tax Range-VIII, in paragraph 11 of the said form/proforma read:

“11. Reasons for the belief that income has escaped assessment.- Information is received from the DIT (Inv.-1), New Delhi that the assessee has introduced money amounting to Rs. 5 lakh during the F.Y. 2002-03 relating to A.Y. 2003-04. Details are contained in Annexure. As per information amount received is nothing but accommodation entry and assessee is a beneficiary.”

9. On the basis of the aforesaid reasons, the Commissioner gave approval recording as under:

“Yes, I am satisfied on the reasons recorded by the A.O. for approval & issue of notice u/s 148 of the I.T Act, 1961.”

10. It is accepted that the Section 151(2) of the Act is applicable in the present case as the proceeding under Section 148 were initiated after expiry of four years from the end of the relevant assessment year. Therefore, the Assessing Officer was required to take approval an officer not below the rank of the Joint Commissioner of Income-Tax after recording reasons. In the present case sanction has been taken from the Commissioner. A Division Bench of Bombay High Court in N.D. Bhatt IAC of IT versus IBM World Trade Corporation, [1995] 216 ITR 811(Bom.) has held as under:

“It is also well-settled that the reasons for reopening are required to be recorded by the assessing authority before issuing any notice under section 148 by virtue of the provisions of section 148(2) at the relevant time. Only the reasons so recorded can be looked at for sustaining or setting aside a notice issued under section 148. In the case of Equitable Investment Co. P. Ltd. v. ITO [1988] 174 ITR 714, a Division Bench of the Calcutta High Court has held that where a notice issued under section 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.”

(emphasis supplied)

11. The aforesaid paragraph in IBM World Trade Corporation (supra) was cited with approval in Prashant S. Joshi versus Income-Tax Officer and Another, 2010 (324) ITR 154 (Bom.) and it was held as under:

“Section 147 provides that 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 163, assess or reassess such income and also any other income chargeable to tax, which has escaped assessment and which comes to his notice subsequently in the course of the proceedings under the section. The first proviso to section 147 has no application in the facts of this case. The basis postulate which underlies section 147 is the formation of the belief by the Assessing Officer that any income chargeable to tax has escaped assessment for any assessment year. The Assessing Officer must have reason to believe that such is the case before he proceeds to issue a notice under section 147. The reasons which are recorded by the Assessing Officer for reopening an assessment are the only reasons which can be considered when the formation of the belief is impugned. The recording of reasons distinguishes an objective from a subjective exercise of power. The requirement of recording reasons is a check against arbitrary exercise of power. For it is on the basis of the reasons recorded and on those reasons alone that the validity of the order reopening the assessment is to be decided. The reasons recorded while reopening the assessment cannot be allowed to grow with age and

ingenuity, by devising new grounds in replies and affidavits not envisaged when the reasons for reopening an assessment were recorded. The principle of law, therefore, is well settled that the question as to whether there was reason to believe, within the meaning of section 147 that income has escaped assessment, must be determined with reference to the reasons recorded by the Assessing Officer. The reasons which are recorded cannot be supplemented by affidavits. The imposition of that requirement ensures against an arbitrary exercise of powers under section 148.”

12. In these circumstances, we are examining the reasons given by the Assessing Officer in the proforma seeking permission/approval of the Commissioner and whether the same satisfy the pre-conditions mentioned in Section 147 of the Act.

13. Annexure attached to the said proforma placed on record of the petitioner reads as under:

“BENEFICIARY’S VALUE OF INSTRUMENT DATE ON NAME ENTRY NO. BY WHICH
TAKEN WHICH ENTRY ENTRY TAKEN
SIGNATURE HOTELS 500000 09-Oct-02 PVT LTD (AC NO-2I060)
NAME OF BANK FROM BRANCH OF A/C NO. ACCOUNT WHICH ENTRY ENTRY
HOLDER OF ENTRY GIVING GIVING ENTRY GIVEN BANK ACCOUNT GIVING
ACCOUNT
SWETU STONE PV SBP DG 50I06”

14. The first sentence of the reasons states that information had been received from Director of Income-Tax (Investigation) that the petitioner had introduced money amounting to Rs.5 lacs during financial year 2002-03 as per the details given in Annexure. The said Annexure, reproduced above, relates to a cheque received by the petitioner on 9th October, 2002 from Swetu Stone PV from the bank and the account number mentioned therein. The last sentence records that as per the information, the amount received was nothing but an accommodation entry and the assessee was the beneficiary.

15. The aforesaid reasons do not satisfy the requirements of Section 147 of the Act. The reasons and the information referred to is extremely scanty and vague. There is no reference to any document or statement, except Annexure, which has been quoted above. Annexure cannot be regarded as a material or evidence that prima facie shows or establishes nexus or link which discloses escapement of income. Annexure is not a pointer and does not indicate escapement of income. Further, it is apparent that the Assessing Officer did not apply his own mind to the information and examine the basis and material of the information. The Assessing Officer accepted the plea on the basis of vague information in a mechanical manner. The Commissioner also acted on the same basis by mechanically giving his approval. The reasons recorded reflect that the Assessing Officer did not independently apply his mind to the information received from the Director of Income-Tax (Investigation) and arrive at a belief whether or not any income had escaped assessment.

16. It may be noted here that a company by the name of Swetu Stone Pvt. Ltd. had applied for and was allotted shares in the petitioner company on payment by cheque of Rs.5 lacs. As noticed

above, in the Annexure the name of the company/account holder is mentioned as Swetu Stone PV. The same is also mentioned in the undated reasons mentioned above.

17. In the counter affidavit it is stated that M/s Swetu Stone Pvt. Ltd. had applied for allotment of shares worth Rs.5 lacs and the same were allotted by the petitioner. It is further stated that statements of Mahesh Garg and Shubhash Gupta were recorded by the Director of Income-Tax (Investigation) and on the basis of the statements they have come to the conclusion that the said persons were entry operators. Copy of the statements of Mahesh Garg and Shubhash Gupta have not been placed on record by the respondent. The petitioner, has, however, enclosed copy of statements of Mahesh Garg and Shubhash Gupta recorded on different dates. The said persons have not specifically named the petitioner though other parties have been named and details have been given and it is stated that they were provided accommodation entries. However, it is stated that the entries were made by giving cheque/DD/PO after receiving cash and sometimes expenses entries were provided. The reasons recorded by the Assessing Officer do not make reference to any statement of Mahesh Garg or Shubhash Gupta. This may not also be necessary, if the statements were on record and it is claimed and prima facie established that they were examined by the Assessing Officer before or at the time of recording reasons. On the other hand, in the present case, information as enclosed as Annexure, has been referred. This is the only material relied upon by the Assessing Officer. The said Annexure has been quoted above. In this connection, we may notice that M/s Swetu Stone Pvt. Ltd. is an incorporated company and the petitioner has pleaded and stated that the said company has a paid-up capital of Rs.90 lacs. The company was incorporated on 4th January, 1989 and was also allotted a permanent account number in September, 2001. To this extent, there is no dispute. In these circumstances, we feel the judgments of the Delhi High Court in Commissioner of Income Tax versus SFIL Stock Broking Limited, [2010] 325 ITR 285 (Delhi) and Sarthak Securities Company Private Limited versus Income Tax Officer, 2010 (329) ITR 110 (Delhi), in which CIT versus Lovely Exports (P) Limited, (2009) 216 CTR 195 (SC) has been applied and followed, are applicable. We may notice here that the respondent in their counter affidavit have stated that Swetu Stone Pvt. Ltd. is unidentifiable and, therefore, the aforesaid decisions should not be applied and the ratio of the decision dated 7th January, 2011 in Writ Petition (Civil) No. 7517/2010, AGR Investment Limited versus Additional Commissioner of Income Tax and Another should be applied. In the said decision, decisions in the case of Sarthak Securities Company Private Limited (supra) and SFIL Stock Broking Limited (supra) was distinguished by giving the following reasons: “22.In SFIL Stock Broking Ltd. (supra), the bench has interfered as it was not discernible whether the assessing officer had applied his mind to the information and independently arrived at a belief on the basis of material which he had before him that the income had escaped assessment. In our considered opinion, the decision rendered therein is not applicable to the factual matrix in the case at hand. In the case of Sarthak Securities Co. Pvt. Ltd. (supra), the Division Bench had noted that certain companies were used as conduits but the Assessee had, at the stage of original assessment, furnished the names of the companies with which it had entered into transaction and the assessing officer was made aware of the situation and further the reason

recorded does not indicate application of mind. That apart, the existence of the companies was not disputed and the companies had bank accounts and payments were made to the Assessee company through the banking channel. Regard being had to the aforesaid fact situation, this Court had interfered. Thus, the said decision is also distinguishable on the factual score.”

18. The facts indicated above do not show that M/s Swetu Stone Pvt. Ltd. is a non-existing and a fictitious entity/person. Decision in AGR Investment Limited (supra), therefore, does not help the case of the respondent.

19. For the reasons stated above, the present writ petition is allowed and writ of certiorari is issued quashing the proceedings under Section 148 of the Act. In the facts of the case, there will be no order as to costs.

SANJIV KHANNA, J.
CHIEF JUSTICE
JULY 21, 2011