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whereby it was stipulated that "the provisions of section 44BB shall not apply in respect of income falling under the provisions of section 44DA". The intention behind insertion of the second proviso to section 44DA was to curtail the applicability of section 44BB. Any interpretation of section 44BB that will render section 44DA as superfluous, must be avoided. He submitted that it is a settled legal position that any interpretation which renders the provision otiose or redundant is to be avoided, and the provision should give a meaningful interpretation. In support of this submission, he placed reliance upon *CWT* v. *Kripashankar Dayashankar Worah* [1971] 81 ITR 763 (SC) and *Sole Trustee, Loka Shikshana Trust* v. *CIT* [1975] 101 ITR 234 (SC). Mr. Bhatia also relied upon the relevant excerpts of the Finance Bill, 2010, to highlight the legislative intent behind insertion of the second proviso to section 44DA.

In so far as the decision of this court in *OHM Ltd.* (supra) is concerned, **10**
he submitted that a special leave petition under article 136 of the Constitution of India had been preferred by the Revenue against the said judgment. Mr. Bhatia further contended that the decision of the Supreme Court in *ONGC* v. *CIT* (supra) must be read in the context of the facts of that case. In the said case, the Supreme Court arrived at a finding that the services provided to the ONGC by contractors did not qualify as "fees for technical services" in view of exclusionary part of *Explanation* 2 to section 9(1)(vii). That being the case, the court held that the services are to be taxed under section 44BB. The question whether the services provided are "royalty", or not, was not an issue before the hon'ble court and hence, the said judgment is not applicable in the facts of the present case. Additionally, he submitted that *ONGC* (supra) applies to assessment years prior to the amendment of 2010 whereby the second proviso to section 44DA was inserted with effect from April 1, 2011. The present case is not weighed down by the *ONGC* case (supra).

*Analysis and conclusion*

*Legal position, viz., section 44BB and section 44DA after amendment introduced under Finance Act, 2010.*

The pivotal controversy in the present case surrounds the interpretation **11**
of sections 44BB and 44DA of the Act. These provisions have undergone amendments over the years, the last one being introduced by the Finance Act, 2010. Since the assessee has argued at length that this legal position remains unaltered, we feel that this aspect in law needs to be clarified as it would also be germane for the decision in the present case. It is, thus, imperative to first examine the effect and consequence of the said amendments, particularly to determine if the legal position has undergone any

change with respect to the applicability of the provisions, after the effective date, i.e., April 1, 2011 since the return of income filed by the petitioner pertains to the assessment year 2012-13. For the sake of convenience, the relevant provisions are reproduced hereunder :

"[1]44BB. *Special provision for computing profits and gains in connection with the business of exploration, etc., of mineral oils*.—(1) Notwithstanding anything to the contrary contained in sections 28 to 41 and sections 43 and 43A, in the case of an assessee, [being a non-resident][2], engaged in the business of providing services or facilities in connection with, or supplying plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of, mineral oils, a sum equal to ten per cent. of the aggregate of the amounts specified in sub-section (2) shall be deemed to be the profits and gains of such business chargeable to tax under the head 'Profits and gains of business or profession' :

Provided that this sub-section shall not apply in a case where the provisions of section 42 or section 44D or [section 44DA or][3] section 115A or section 293A apply for the purposes of computing profits or gains or any other income referred to in those sections.

(2) The amounts referred to in sub-section (1) shall be the following, namely :—

(a) the amount paid or payable (whether in or out of India) to the assessee or to any person on his behalf on account of the provision of services and facilities in connection with, or supply of plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of, mineral oils in India ; and

(b) the amount received or deemed to be received in India by or on behalf of the assessee on account of the provision of services and facilities in connection with, or supply of plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of, mineral oils outside India.

(3) Notwithstanding anything contained in sub-section (1), an assessee may claim lower profits and gains than the profits and gains specified in that sub-section, if he keeps and maintains such books of account and other documents as required under sub-section (2) of section 44AA and gets his accounts audited and furnishes a report of such audit as required under section 44AB, and thereupon the

1. Inserted by the Finance Act, 1987 w.r.e.f. April 1, 1983.
2. Inserted by the Finance Act, 1988, w.r.e.f. April 1, 1983.
3. Inserted by Finance Act, 2010, with effect form April 1, 2011.

Assessing Officer shall proceed to make an assessment of the total income or loss of the assessee under sub-section (3) of section 143 and determine the sum payable by, or refundable to, the assessee.

*Explanation*.—For the purposes of this section,—

(i) 'plant' includes ships, aircraft, vehicles, drilling units, scientific apparatus and equipment, used for the purposes of the said business ;

(ii) 'mineral oil' includes petroleum and natural gas.

44DA. *Special provision for computing income by way of royalties, etc., in case of non-residents*.[1]—(1) The income by way of royalty or fees for technical services received from Government or an Indian concern in pursuance of an agreement made by a non-resident (not being a company) or a foreign company with Government or the Indian concern after the 31st day of March, 2003, where such non-resident (not being a company) or a foreign company carries on business in India through a permanent establishment situated therein, or performs professional services from a fixed place of profession situated therein, and the right, property or contract in respect of which the royalties or fees for technical services are paid is effectively connected with such permanent establishment or fixed place of profession, as the case may be, shall be computed under the head 'Profits and gains of business or profession' in accordance with the provisions of this Act :

Provided that no deduction shall be allowed,—

(i) in respect of any expenditure or allowance which is not wholly and exclusively incurred for the business of such permanent establishment or fixed place of profession in India ; or

(ii) in respect of amounts, if any, paid (otherwise than towards reimbursement of actual expenses) by the permanent establishment to its head office or to any of its other offices :

[*Provided further that the provisions of section 44BB shall not apply in respect of the income referred to in this section*.][2]"

Therefore, if, inter alia, section 44DA applies for the purpose of computing profits or gains or any other income referred to in section 44DA, then sub-section (1) of section 44BB would not apply. The nature of income dealt with by section 44DA is either royalty, or fees for technical services.

1. Inserted by Finance Act, 2003 w.e.f 1-04-2004.
2. Inserted by Finance Act, 2010 w.e.f 1-04-2011.

Thus, it needs examination whether the nature of income derived by the petitioner either qualifies as "royalty" or "fees for technical services".

**12** Section 9 of the Act deals with "Income deemed to accrue or arise in India". The relevant extract of section 9(1)(vi) and 9(1)(vii) read as follows :

"9(1) The following incomes shall be deemed to accrue or arise in India : . . .

(vi) income by way of royalty payable by—

(a) the Government ; or

(b) a person who is a resident, except where the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India ; or

(c) a person who is a non-resident, where the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India :

Provided that nothing contained in this clause shall apply in relation to so much of the income by way of royalty as consists of lump sum consideration for the transfer outside India of, or the imparting of information outside India in respect of, any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula or process or trade mark or similar property, if such income is payable in pursuance of an agreement made before the 1st day of April, 1976, and the agreement is approved by the Central Government :

Provided further that nothing contained in this clause shall apply in relation to so much of the income by way of royalty as consists of lump sum payment made by a person, who is a resident, for the transfer of all or any rights (including the granting of a licence) in respect of computer software supplied by a non-resident manufacturer along with a computer or computer-based equipment under any scheme approved under the Policy on Computer Software Export, Software Development and Training, 1986 of the Government of India."

*Explanations 2 to 6* to section 9(1)(vi) are relevant and read as follows :

"*Explanation 2.*—For the purposes of this clause, 'royalty' means consideration (including any lump sum consideration but excluding

any consideration which would be the income of the recipient chargeable under the head 'Capital gains') for—

(i) the transfer of all or any rights (including the granting of a licence) in respect of a patent, invention, model, design, secret formula or process or trade mark or similar property ;

(ii) the imparting of any information concerning the working of, or the use of, a patent, invention, model, design, secret formula or process or trade mark or similar property ;

(iii) the use of any patent, invention, model, design, secret formula or process or trade mark or similar property ;

(iv) the imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill ;

(iva) the use or right to use any industrial, commercial or scientific equipment but not including the amounts referred to in section 44BB ;

(v) the transfer of all or any rights (including the granting of a licence) in respect of any copyright, literary, artistic or scientific work including films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting, but not including consideration for the sale, distribution or exhibition of cinematographic films ; or

(vi) the rendering of any services in connection with the activities referred to in sub-clauses (i) to (iv), (iva) and (v).

Explanation 3.—*For the purposes of this clause, 'computer software' means any computer programme recorded on any disc, tape, perforated media or other information storage device and includes any such programme or any customized electronic data.*

Explanation 4.—*For the removal of doubts, it is hereby clarified that the transfer of all or any rights in respect of any right, property or information includes and has always included transfer of all or any right for use or right to use a computer software (including granting of a licence) irrespective of the medium through which such right is transferred.*

Explanation 5.—For the removal of doubts, it is hereby clarified that the royalty includes and has always included consideration in respect of any right, property or information, whether or not—

(a) the possession or control of such right, property or information is with the payer ;

(b) such right, property or information is used directly by the payer ;

(c) the location of such right, property or information is in India.

*Explanation 6*.—For the removal of doubts, it is hereby clarified that the expression 'process' includes and shall be deemed to have always included transmission by satellite (including up-linking, amplification, conversion for down-linking of any signal), cable, optic fibre or by any other similar technology, whether or not such process is secret ;" (emphasis[1] supplied)

Section 9(1)(vii) deals with "income by way of fees for technical services" and reads as follows :

"(vii) income by way of fees for technical services payable by—

(a) the Government ; or

(b) a person who is a resident, except where the fees are payable in respect of services utilised in a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India ; or

(c) a person who is a non-resident, where the fees are payable in respect of services utilised in a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India :

Provided that nothing contained in this clause shall apply in relation to any income by way of fees for technical services payable in pursuance of an agreement made before the 1st day of April, 1976, and approved by the Central Government.

*Explanation 1*.—For the purposes of the foregoing proviso, an agreement made on or after the 1st day of April, 1976, shall be deemed to have been made before that date if the agreement is made in accordance with proposals approved by the Central Government before that date.

*Explanation 2*.—For the purposes of this clause, 'fees for technical services' means any consideration (including any lump sum consideration) for the rendering of any managerial, technical or consultancy services (including the provision of services of technical or other personnel) but does not include consideration for any construction, assembly, mining or like project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head 'Salaries'."

The interplay between section 44DA(1) and section 44BB(1) of the Act has been a subject matter of several judgments. We need not engage

1. Here printed in italics.

ourselves with an elaborate analysis of the said provisions, as they existed prior to amendments, and it would suffice to note that the conflict between the two provisions has been noticed in several decisions. The Revenue has always maintained its stand that both set of provisions are special in nature which operate in their own clearly defined spheres ; once a particular receipt of income takes on the character of royalty/fees for technical service as defined in section 9(1)(vi)/9(1)(vii), it cannot be considered for treatment under section 44BB and has to be taxed under section 115A/44DA of the Act. That being said, there are several judgments of this court, wherein it has been held that section 44BB is a specific provision and in case the income falls within the ambit of section 44DA(1) of the Act, it would be liable to be taxed under section 44BB(1) of the Act, provided it was in connection with extraction or production of mineral oils. This conflict or inconsistency now stands resolved by virtue of the amendments introduced under the Finance Act, 2010. Though the insertions are stated to be clarificatory, however the rationale behind the introduction of the amendments has to be examined to appreciate the legislative intent envisioned under the Finance Act, 2010.

Section 44BB is a special provision for computing profits and gains of a **13**
non-resident from business of providing services or facilities in connection with, or supplying plant and machinery on hire, used or to be used in the prospecting for or extraction or production of mineral oils, including petroleum and natural gas. Section 44DA is broader and more general in nature and provides for assessment of the income of the non-resident by way of royalty or fees for technical services, where such non-resident carries on business in India through a permanent establishment situated therein, or performs services from a fixed place of profession situated in India and the right, property or contract in respect of which the royalties or fees for technical services are paid is effectively connected with the permanent establishment or fixed place of profession situated in India. One more distinction between sections 44DA and 44BB is that, in section 44BB one does not find any reference to a permanent establishment in India and the services contemplated therein are more specific than what is contemplated in section 44DA. Thus, section 44BB is a special provision in so far as it relates to the applicability of the provision in the context of the specified services. Section 44DA applies where such non-resident carries on business in India through a permanent establishment stipulated therein or performs services from a fixed place of profession, such income shall be computed under the head "Profits and gains of business or profession" in accordance with the provisions of the Act, subject to the condition that no deduction shall be

allowed in respect of any expenditure or allowance which is not wholly or exclusively incurred for the business of such permanent establishment or fixed place of profession in India or in respect of amounts, if any, paid by the permanent establishment to its head office or to any of its other offices. Section 115A of the Act provides the rate of taxation in respect of income of a non-resident, in the nature of royalty or fees for technical services, other than the income referred in section 44DA, i.e., income in the nature of royalty and fees for technical services which is not connected with the permanent establishment of the non-resident.

**14** There is another section that needs to be referred, for the sake of comprehensive understanding, i.e., section 44D of the Act, inserted in the first place vide Finance Act, 1976[1] for taxability of income in the nature of royalty and fee for technical services. Later, a special provision was introduced by way of section 44BB vide Finance Act, 1987. However, even when section 44D was appearing in the statute book, section 44BB contained a proviso which excluded applicability of section 44BB to cases that were covered by section 44D. However, it is pertinent to note that there was no similar proviso appearing under section 44D. Finance Act, 2003 provided a

1. For the sake of reference, the same is reproduced as under :

"44D. *Special provision for computing income by way of royalties, etc., in the case of foreign companies.*—Notwithstanding anything to the contrary contained in sections 28 to 44C, in the case of an assessee, being a foreign company,—

(a) the deductions admissible under the said sections in computing the income by way of royalty or fees for technical services received from an Indian concern in pursuance of an agreement made by the foreign company with the Indian concern before the 1st day of April, 1976, shall not exceed in the aggregate twenty per cent. of the gross amount of such royalty or fees as reduced by so much of the gross amount of such royalty as consists of lump sum consideration for the transfer outside India of, or the imparting of information outside India in respect of, any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula or process or trade mark or similar property ;

(b) no deduction in respect of any expenditure or allowance shall be allowed under any of the said sections in computing the income by way of royalty or fees for technical services received from an Indian concern in pursuance of an agreement made by the foreign company with the Indian concern after the 31st day of March, 1976.

*Explanation*.—For the purposes of this section,—

(a) 'fees for technical services' shall have the same meaning as in Explanation to clause (vii) of sub-section (1) of section 9 ;

(b) 'foreign company' shall have the same meaning as in section 80B ;

(c) 'royalty' shall have the same meaning as in the Explanation to clause (vi) of sub-section (1) of section 9 ;

(d) royalty received from an Indian concern in pursuance of an agreement made by a foreign company with the Indian concern after the 31st day of March, 1976, shall be deemed to have been received in pursuance of an agreement made before the 1st day of April, 1976, if such agreement made is deemed, for the purposes of the proviso to clause (vi) of sub-section (1) of section 9, to have been made before the 1st day of April, 1976."

sunset clause to the operation of section 44D with effect from 1st April 2003. Simultaneously, from the said date, a similar provision by way of section 44DA was introduced. It is significant to note that both the provisions, i.e., section 44D as well as section 44DA pertain to the same subject matter, i.e., taxation of income by way of "royalties and fees for technical services".

The aforesaid provisions further underwent change by way of amend- **15**
ments introduced by the Finance Act, 2010, with effect from April 1, 2011. By way of the said Act, a reference to section 44DA was inserted in the proviso to sub section (1) of section 44BB. Simultaneously, a second proviso to sub section (1) of section 44DA was inserted to the following effect :

> "Provided further that provisions of section 44BB shall not apply in respect of the income referred to in this section".

Keeping in mind the legislative history of amendments in the two pro- **16**
visions, the aforesaid amendments are significant and changed the position with respect to the applicability of the said provisions. A taxing statute is to be construed strictly. The position that existed prior to the amendments was different. There was no proviso which restricted the applicability of section 44BB in respect of the income falling within the scope of section 44DA(1) of the Act. However, now that the proviso has been inserted, it has fundamentally restricted the applicability of section 44BB. This proviso has to be given due consideration and a meaning, recognizing the legislative intent. A plain reading of section 44BB(1) shows that it applies to an assessee who is engaged in the business of providing services or facilities in connection with, or supplying plant and machinery on hire use, or to be used, in the prospecting for, or extraction or production of mineral oils. However, the proviso thereto carves out an exception that the sub-section shall not apply in a case where the provisions of section 44DA apply for the purpose of computing profits or gains or any other income referred to in those sections. Further, a reading of section 44DA makes it clear that it applies to the character of income which is in the nature of royalty or fees for technical services. The legislative intent behind the amendment is also evident from the memorandum to the Finance Bill 2010 ([2010] 321 ITR (St.) 110) which reads as under :

> "Under the existing provisions contained in section 44BB(1) of the Income-tax Act, income of a non-resident taxpayer who is engaged in the business of providing services or facilities in connection with, or supplying plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of, mineral oils is computed at ten per cent of the aggregate of the amounts paid.

Section 44DA provides the procedure for computing income of a non-resident, including a foreign company, by way of royalty or fee for technical services, in case the right, property or contract giving rise to such income are effectively connected with the permanent establishment of the said non-resident. This income is computed as per the books of account maintained by the assessee.

Section 115A provides the rate of taxation in respect of income of a non-resident, including a foreign company, in the nature of royalty or fee for technical services, other than the income referred to in section 44DA, i.e., income in the nature of royalty and fee for technical services which is not connected with the permanent establishment of the non-resident.

Combined effect of the provisions of sections 44BB, 44DA and 115A is that if the income of a non-resident is in the nature of fee for technical services, it shall be taxable under the provisions of either section 44DA or section 115A irrespective of the business to which it relates. *Section 44BB applies only in a case where consideration is for services and other facilities relating to exploration activity which are not in the nature of technical services. However, owing to judicial pronouncements, doubts have been raised regarding the scope of section 44BB vis-a-vis section 44DA as to whether fee for technical services relating to the exploration sector would also be covered under the presumptive taxation provisions of section 44BB.*

*In order to remove doubts and clarify the distinct scheme of taxation of income by way of fee for technical services, it is proposed to amend the proviso to section 44BB so as to exclude the applicability of section 44BB to the income which is covered under section 44DA. Similarly, section 44DA is also proposed to be amended to provide that provisions of section 44BB shall not apply to the income covered under section 44DA.*

These amendments are proposed to take effect from April 1, 2011 and will, accordingly, apply in relation to the assessment year 2011-12 and subsequent years."

This proviso reinforces the legislative intent to carve out an exception to the character of the income referred to in this section, i.e., royalty and fees for technical services. The principles relating to interpretation of statute, emphatically lay down that statute should be interpreted to preserve the legislative intent. A reading of the overall scheme of sections 44BB and 44DA leaves no manner of doubt that section 44BB applies if the assessee is engaged in the business of providing services or facilities in the

prospecting for, or extraction or production of mineral oils. However, if income earned by such assessee takes the colour of royalty or fee for technical services, then the computation for the purposes of determining "profits and gains of business or profession" is to be done as per the provisions of section 44DA of the Act. Therefore, now in the current scenario if the income of the assessee is royalty or fees for technical services , then the same would be taxed under section 9(1)(vi)/(vii) read with section 115A or section 44DA, as the case may be.

*Judgments relied upon by the parties*

Now, let us reflect upon the case law relied upon by the parties. In *Oil* **17** *and Natural Gas Corporation* v. *CIT* (supra), the "pith and substance" test was applied in respect of the position that existed prior to the amendments taken note of hereinabove and, therefore, the said judgment does not deal with the situation that we are faced with on question of interplay of the two provisions. Furthermore, in the said case, the Supreme Court concluded that the services provided to ONGC by contractors in the batch of appeals do not qualify as fees for technical services, in view of the exclusionary part of *Explanation 2* to section 9(1)(vii). In that view of the matter, the court held that the services are to be taxed under section 44BB. The court, thus did not have the occasion to consider the import, effect and purpose of proviso to section 44BB, that existed during the relevant time. This is evident from the following observations made in the said judgment (page 314 of 376 ITR) :

> "A careful reading of the aforesaid provisions of the Act goes to show that under section 44BB(1) in the case of a non-resident providing services or facilities in connection with or supplying plant and machinery used or to be used in prospecting, extraction or production of mineral oils the profit and gains from such business chargeable to tax is to be calculated at a sum equal to 10 per cent. of the aggregate of the amounts paid or payable to such non-resident assessee as mentioned in sub-section (2). On the other hand, section 44D contemplates that if the income of a foreign company with which the Government or an Indian concern had an agreement executed before April 1, 1976, or on any date thereafter the computation of income would be made as contemplated under the aforesaid section 44D. *Explanation (a)* to section 44D, however, specifies that 'fees for technical services' as mentioned in section 44D would have the same meaning as in *Explanation 2* to clause (vii) of section 9(1). The said *Explanation*, as quoted above, defines 'fees for technical services' to mean consideration for rendering of any managerial, technical or con-

sultancy services. However, the later part of the *Explanation* excludes from consideration for the purposes of the expression, i.e., 'fees for technical services' any payment received for construction, assembly, mining or like project undertaken by the recipient or consideration which would be chargeable under the head 'Salaries'. Fees for technical services, therefore, by virtue of the aforesaid *Explanation* will not include payments made in connection with a mining project . . .

The Income-tax Act does not define the expressions 'mines' or 'minerals'. The said expressions are found defined and explained in the Mines Act, 1952, and the Oil Fields (Development and Regulation) Act, 1948. While construing the somewhat pari materia expressions appearing in the Mines and Minerals (Development and Regulation) Act, 1957, regard must be had to the provisions of entries 53 and 54 of List I and Entry 22 of List II of the Seventh Schedule to the Constitution to understand the exclusion of mineral oils from the definition of minerals in section 3(a) of the 1957 Act. Regard must also be had to the fact that mineral oils is separately defined in section 3(b) of the 1957 Act to include natural gas and petroleum in respect of which Parliament has exclusive jurisdiction under entry 53 of List I of the Seventh Schedule and had enacted an earlier legislation, i.e., the Oil Fields (Regulation and Development) Act, 1948. Reading section 2(j) and section 2(jj) of the Mines Act, 1952, which define mines and minerals and the provisions of the Oil Fields (Regulation and Development) Act, 1948, specifically relating to prospecting and exploration of mineral oils, exhaustively referred to earlier, it is abundantly clear that drilling operations for the purpose of production of petroleum would clearly amount to a mining activity or a mining operation. Viewed thus, it is the proximity of the works contemplated under an agreement, executed with a non-resident assessee or a foreign company, with mining activity or mining operations that would be crucial for the determination of the question whether the payments made under such an agreement to the non-resident assessee or the foreign company is to be assessed under section 44BB or section 44D of the Act. The test of pith and substance of the agreement commends to us as reasonable for acceptance. Equally important is the fact that the Central Board of Direct Taxes had accepted the said test and had in fact issued a circular as far back as October 22, 1990, to the effect that mining operations and the expressions 'mining projects' or 'like projects' occurring in *Explanation* 2 to section 9(1) of the Act would cover rendering of service like imparting of training and

carrying out drilling operations for exploration of and extraction of oil and natural gas and, hence, payments made under such agreement to a non-resident/foreign company would be chargeable to tax under the provisions of section 44BB and not section 44D of the Act. We do not see how any other view can be taken if the works or services mentioned under a particular agreement is directly associated or inextricably connected with prospecting, extraction or production of mineral oils. Keeping in mind the above provision, we have looked into each of the contracts involved in the present group of cases and find that the brief description of the works covered under each of the said contracts as culled out by the appellants and placed before the court is correct. The said details are set out below :

| *S. No.* | *Civil Appeal No.* | *Work covered under* |
|---|---|---|
| 1. | 4321 | Drilling of exploration wells and carrying out seismic surveys for exploratory drilling. |
| 2. | 740 | Drilling, furnishing personnel for manning, maintenance and operation of drilling rig and training of personnel. |
| 3. | 731 | Drilling, furnishing personnel for manning, maintenance and operation of drilling rig and training of personnel. |
| 4. | 1722 | Furnishing supervisory staff with expertise in operation and management of drilling unit. |
| 5. | 729 | Capping including subduing of well, fire fighting. |
| 6. | 738 | Capping including subduing of well, fire fighting. |
| 7. | 1528 | Analysis of data to prepare job design, procedure for execution and details regarding monitoring. |
| 8. | 1532 | Study for selection of enhanced oil recovery processes and conceptual design of pilot tests. |
| 9. | 1520 | Engineering and technical support to ONGC in implementation of cyclic steam stimulation in heavy oil wells. |
| 10. | 2794 | Assessment and processing of seismic data along with engineering and technical support in implementation of cyclic steam stimulation. |
| 11. | 1524 | Conducting reservoir stimulation studies in association with personnel of ONGC. |
| 12. | 1535 | Laboratory testing under simulated reservoir conditions. |
| 13. | 1514 | Consultancy for optimal exploitation of hydrocarbon resources. |
| 14. | 2797 | Consultancy for all aspects of coal bed methane. |
| 15. | 6174 | Analysis of data of wells to prepare a job design. |
| 16. | 1517 | Geological study of the area and analysis of seismic information reports to design 2 dimensional seismic surveys. |

| | | |
|---|---|---|
| 17. | 7226 | Opinion on hydrocarbon resources and foreseeable potential. |
| 18. | 7227 | Opinion on hydrocarbon resources and foreseeable potential. |
| 19. | 7230 | Opinion on hydrocarbon resources and foreseeable potential. |
| 20. | 6016 | Opinion on hydrocarbon resources and foreseeable potential. |
| 21. | 6008 | Evaluation of ultimate resource potential and presentations outside India in connection with promotional activities for joint venture exploration program. |
| 22. | 1531 | Review of sub-surface well data, provide repair plan of wells and supervise repairs. |
| 23. | 733 | Repair of gas turbine, gas control system and inspection of gas turbine and generator. |
| 24. | 741 | Repair and inspection of turbines. |
| 25. | 737 | Repair, inspection and overhauling of turbines. |
| 26. | 736 | Inspection, engine performance evaluation, instrument calibration and inspection of far turbines. |
| 27. | 1522 | Replacement of choke and kill consoles on drilling rigs. |
| 28. | 1521 | Inspection of gas generators. |
| 29. | 1515 | Inspection of rigs. |
| 30. | 2012 | Inspection of generator. |
| 31. | 1240 | Inspection of existing control system and deputing engineer to attend to any problem arising in the machines. |
| 32. | 1529 | Inspection of drilling rig and verification of reliability of control systems in the drilling rig. |
| 33. | 2008 | Expert advice on the device to clean insides of a pipeline. |
| 34. | 2795 | Feasibility study of rig to assess its remaining useful life and to carry out structural alterations. |
| 35. | 925 | Engineering analysis of rig. |
| 36. | 1519 | Imparting training on cased hold production log evaluation and analysis. |
| 37. | 1533 | Training on well control. |
| 38. | 1518 | Training on implementation of six sigma concepts. |
| 39. | 1516 | Training on implementation of six sigma concepts. |
| 40. | 6023 | Training on drilling project management. |
| 41. | 2796 | Training in safety rating system and assistance in development and audit of safety management system. |
| 42. | 1239 | To develop technical specification for 3D seismic API modules of work and to prepare bid packages. |
| 43. | 1527 | Supply supervision and installation of software which is used for analysis of flow rate of mineral oil to determine reservoir conditions. |
| 44. | 1523 | Supply, installation and familiarization of software for processing seismic data. |

*The above facts would indicate that the pith and substance of each of the contracts/agreements is inextricably connected with prospecting, extraction or production of mineral oil. The dominant purpose of each of such agreement is for prospecting, extraction or production of mineral oils though there may be certain ancillary works contemplated thereunder. If that be so, we will have no hesitation in holding that the payments made by ONGC and received by the non-resident assessees or foreign companies under the said contracts is more appropriately assessable under the provisions of section 44BB and not section 44D of the Act.* On the basis of the said conclusion reached by us, we allow the appeals under consideration by setting aside the orders of the High Court passed in each of the cases before it and restoring the view taken by the learned Appellate Commissioner as affirmed by the learned Tribunal. (emphasis[1] supplied)

The above noted judgment assumes significance, though on a different aspect, which we shall elucidate and expound later in this judgment.

The judgment of this court in *DIT* v. *OHM Ltd.* [2013] 352 ITR 406 **18**
(Delhi) also does not help the petitioner. In the said case, the assessee was engaged in the business of providing geophysical services to oil and gas exploration industry ; conducting electromagnetic, processing and interpretation of data, which so collected through the survey was used in offshore oil industry. In the said case, the assessee claimed that the oil and gas exploration activity was directly related and was part of exploration/ prospecting activities for mineral oil and such services fell within the ambit of section 44BB. Authority for Advance Ruling followed its earlier decision and decided in favour of the assessee. The Revenue in the challenge, contended that the authority had erred in having failed to note that the appropriate provision to be applied was section 44DA read with section 9(1)(vii), *Explanation 2* of the Act. The court in the said case agreed with the view taken by the Authority for Advance Rulings and referred to its earlier decisions of *DIT* v. *Jindal Drilling and Industries Ltd.* [2010] 320 ITR 104 (Delhi) and also to another order of the Authority for Advance Rulings in the case of *Geofizyka Torun sp. Z.O.O. In Re* [2010] 320 ITR 268 (AAR), and concluded that the view taken by the Authority was correct and held that section 44DA is broader in scope as compared to section 44BB. In that context, the court considered the effect of second proviso to sub-section (1) of section 44DA inserted by the Finance Act, 2010 and held as under (page 416 of 352 ITR) :

1. Here printed in italics.

"We do not think that there is any error in the view taken by Authority for Advance Rulings. Basically the rule that the specific provision excludes the general provision has been applied. Section 44BB is a special provision for computing the profits and gains of a non-resident in connection with the business of providing services or facilities in connection with, or supplying plant and machinery on hire, used or to be used, in the prospecting for, or extraction or production of mineral oils including petroleum and natural gas. Section 44DA is also a provision which applies to non-residents only. It is, however, broader and more general in nature and provides for assessment of the income of the non-resident by way of royalty or fees for technical services, where such non-resident carries on business in India through a permanent establishment situated therein or performs services from a fixed place of profession situated in India and the right, property or contract in respect of which the royalties or fees for technical services are paid is effectively connected with the permanent establishment or fixed place of profession. Such income would be computed and assessed under the head "Business" in accordance with the provisions of the Act, subject to the condition that no deduction would be allowed in respect of any expenditure or allowance which is not wholly or exclusively incurred for the business of such permanent establishment or fixed place of profession or in respect of amounts, if any, paid by the permanent establishment to its head office or to any of its other offices. Under section 44BB, one does not find any reference to a permanent establishment in India. The type of services contemplated by the provision is more specific than what is contemplated by section 44DA. Section 44BB refers specifically to 'services or facilities in connection with, or supplying plant and machinery on hire, used or to be used in the prospecting for, or extraction or production of mineral oils'. Revenues earned by the non-resident from rendering such specific services are covered by section 44BB. It is a well settled rule of interpretation that if a special provision is made respecting a certain matter, that matter is excluded from the general provision under the rule which is expressed by the maxim 'generalia specialibus non derogant'. It is again a well-settled rule of construction that when, in an enactment two provisions exist, which cannot be reconciled with each other, they should be so interpreted that, if possible, effect should be given to both. This was stated to be the 'rule of harmonious construction' by the Supreme Court in *Venkataramana Devaru* v. *State of Mysore*, AIR 1958 SC 255.

If as contended by the Revenue, section 44DA covers all types of services rendered by the non-resident, that would reduce section 44BB to a useless lumber or dead letter and such a result would be opposed to the very essence of the rule of harmonious construction. In *South India Corporation (P.) Ltd.* v. *Secretary, Board of Revenue, Trivandrum*, AIR 1964 SC 207, it was held that a familiar approach in such cases is to find out which of the two apparently conflicting provisions is more general and which is more specific and to construe the more general one as to exclude the more specific.

The second proviso to sub-section (1) of section 44DA inserted by the Finance Act, 2010, with effect from April 1, 2011, makes the position clear. Simultaneously, a reference to section 44DA was inserted in the proviso to sub-section (1) of section 44BB. It should be remembered that section 44DA also requires that the non-resident or the foreign company should carry on business in India through a permanent establishment situated therein and the right, property or contract in respect of which the royalty or fees for technical services is paid should be effectively connected with the permanent establishment. Such a requirement has not been spelt out in section 44BB ; moreover, a flat rate of 10 per cent. of the revenues received by the non-resident for the specific services rendered by it are deemed to be profits from the business chargeable to tax in India under section 44BB, whereas under section 44DA, deduction of expenditure or allowance wholly and exclusively incurred by the non-resident for the business of the permanent establishment in India and for expenditure towards reimbursement of actual expenses by the permanent establishment to its head office or to any of its other offices is allowed from the revenues received by the non-resident. Because of the different modes or methods prescribed in the two sections for computing the profits, it apparently became necessary to clarify the position by making necessary amendments. That perhaps is the reason for inserting the second proviso to sub-section (1) of section 44DA and a reference to section 44DA in the proviso below sub-section (1) of section 44BB. A careful perusal of both the provisos shows that they refer only to computation of the profits under the sections. If both the sections have to be read harmoniously and in such a manner that neither of them becomes a useless lumber then the only way in which the provisos can be given effect to is to understand them as referring only to the computation of profits, and to understand the amendments as having been inserted only to clarify the position. *So understood, the*

*proviso to sub-section (1) of section 44BB can only mean that the flat rate of 10 per cent. of the revenues cannot be deemed to be the profits of the non-resident where the services are of the type which do not fall under that section, but are more general in nature so as to fall under section 44DA. Similarly, the second proviso to sub-section (1) of section 44DA can only be interpreted to mean that where the services are general in nature and fall under the sub-section read with* Explanation 2 *to section 9(1)(vii) of the Act, then an assessee rendering such services as provided in section 44BB cannot claim the benefit of being assessed on the basis that 10 per cent. of the revenues will be deemed to be the profits as provided in section 44BB. In other words, the amendment made by the Finance Act, 2010, with effect from April 1, 2011, in both the sections, cannot have the effect of altering or effacing the fundamental nature of both the provisions or their respective spheres of operation or to take away the separate identity of section 44BB. We do not, therefore, see how these amendments can assist the Revenue's contention in the present case, put forward by the learned senior standing counsel. We, therefore, agree with the Authority for Advance Rulings that in the present case the profits shall be computed in accordance with the provisions of section 44BB of the Act and not section 44DA.*

In the result the writ petition fails and is dismissed with no order as to costs." (emphasis[1] supplied)

**19** The petitioner has strongly relied upon the aforesaid observations to argue that this court had explicated that the second proviso does not efface the applicability of section 44BB, and notwithstanding the second proviso to section 44DA, the legal position remains unaffected. Before commenting on this contention, it is also necessary to take note of a later decision of this court in *PGS Exploration (Norway) AS* v. *Addl. DIT* [2016] 383 ITR 178 (Delhi), where the court also had the occasion to consider the aforesaid case of *DIT* v. *OHM Ltd.* (supra). In the said case, the court upheld the contention advanced on behalf of the assessee that since it is engaged in the business of providing services in connection with prospecting for mineral oils, its income, even if it falls within the ambit of section 44DA(1) of the Act, would be taxable under section 44BB(1). However, at the same time, the court considered the effect of the amendments introduced by the Finance Act, 2010 and held as under (page 193 of 383 ITR) :

"The contention advanced on behalf of the Revenue that 'fees for technical services' earned by a foreign company in respect of a

1. Here printed in italics.

contract which is connected with the permanent establishment of such foreign company in India would be taxable under section 44DA(1) of the Act, irrespective of whether the same is connected with extraction or production of mineral oils, cannot be accepted. By virtue of Finance Act, 2003, such income was excluded from the ambit of section 115A(1)(b) of the Act, with effect from April 1, 2004. Although, with effect from the said date such income was taxable under section 44DA(1) of the Act but in certain cases where such income was earned by the assessee by carrying on a business of providing services in connection with prospecting for, or extraction or production of mineral oils, the said income would also fall within the express language of section 44BB(1) of the Act and in view of the decision of this court in *OHM* (supra), the provisions of section 44BB(1) of the Act would be applied in preference to section 44DA(1) of the Act, in those cases. This conflict between section 44BB(1) and section 44DA(1) of the Act was resolved by the Finance Act, 2010 by including a reference to section 44DA in the proviso to section 44BB(1) of the Act with effect from April 1, 2011 and simultaneously introducing a second proviso to section 44DA(1) which reads as under :

'Provided further that the provisions of section 44BB shall not apply in respect of the income referred to in this section.'

*Thus, after April 1, 2011, income falling within the scope of section 44DA(1) of the Act would be excluded from the scope of section 44BB of the Act. However during the period from April 1, 2004 to April 1, 2011 tax on any income from fees for technical services falling within section 44DA(1) of the Act—which was excluded from the ambit of section 115A(1)(b) of the Act but was not expressly excluded from the scope of section 44BB(1) of the Act—would be computed under section 44BB(1) of the Act. Since the assessment year 2008-09 falls within this period, the income of the assessee, to the extent it falls within the scope of section 44DA(1) of the Act and stands excluded from section 115A(1)(b) of the Act, would be computed in accordance with section 44BB(1) of the Act.*

Having stated the above, we must clarify that the income falling within section 115A(1)(b) of the Act which does not fall within the four corners of section 44DA(1) of the Act would also not be taxable under section 44BB(1) of the Act, for the reason that by virtue of proviso to section 44BB(1) of the Act, it is expressly excluded. Accordingly, if the consideration received by the assessee for services

rendered is found to be 'fees for technical services', the Assessing Officer would specifically have to determine (a) whether the assessee had a permanent establishment in India during the relevant period ; and (b) if so, whether the contracts entered into by the appellant with BG and RIL were effectively connected with the assessee's permanent establishment in India. It is only, if the Assessing Officer finds that the said two conditions are satisfied, that the income of the assessee would be computed under section 44BB(1) of the Act. However, if such conditions are not satisfied then the income-tax payable by the appellant would have to be computed in accordance with section 115A(1)(b) of the Act."

**20** The aforesaid observations, in our view, rightly interpret the position in law. For that matter, the petitioner is misinterpreting the earlier judgment of this court in *DIT* v. *OHM* (supra), to contend that section 44BB being a specific provision will override the provisions of section 44DA of the Act. Section 44BB of the Act qualifies a business activity whilst section 44DA applies to the nature of income. Even in *OHM Ltd.* (supra), the court has taken a view that is in concurrence with our opinion. In the said judgment, the court in para 12 notes as under (page 417 of 352 ITR) :

"The second proviso to sub-section (1) of section 44DA inserted by the Finance Act, 2010, with effect from April 1, 2011, makes the position clear. Simultaneously, a reference to section 44DA was inserted in the proviso to sub-section (1) of section 44BB. It should be remembered that section 44DA also requires that the non-resident or the foreign company should carry on business in India through a permanent establishment situated therein and the right, property or contract in respect of which the royalty or fees for technical services is paid should be effectively connected with the permanent establishment. Such a requirement has not been spelt out in section 44BB ; moreover, a flat rate of 10 per cent. of the revenues received by the non-resident for the specific services rendered by it are deemed to be profits from the business chargeable to tax in India under section 44BB, whereas under section 44DA, deduction of expenditure or allowance wholly and exclusively incurred by the non-resident for the business of the permanent establishment in India and for expenditure towards reimbursement of actual expenses by the permanent establishment to its head office or to any of its other offices is allowed from the revenues received by the non-resident. Because of the different modes or methods prescribed in the two sections for computing the profits, it apparently became necessary to clarify the position by

making necessary amendments. That perhaps is the reason for inserting the second proviso to sub-section (1) of section 44DA and a reference to section 44DA in the proviso below sub-section (1) of section 44BB. A careful perusal of both the provisos shows that they refer only to computation of the profits under the sections. If both the sections have to be read harmoniously and in such a manner that neither of them becomes a useless lumber then the only way in which the provisos can be given effect to is to understand them as referring only to the computation of profits, and to understand the amendments as having been inserted only to clarify the position. So understood, the proviso to sub-section (1) of section 44BB can only mean that the flat rate of 10 per cent. of the revenues cannot be deemed to be the profits of the non-resident where the services are of the type which do not fall under that section, but are more general in nature so as to fall under section 44DA. Similarly, the second proviso to sub-section (1) of section 44DA can only be interpreted to mean that where the services are general in nature and fall under the sub-section read with *Explanation 2* to section 9(1)(vii) of the Act, then an assessee rendering such services as provided in section 44BB cannot claim the benefit of being assessed on the basis that 10 per cent. of the revenues will be deemed to be the profits as provided in section 44BB. In other words, the amendment made by the Finance Act, 2010, with effect from April 1, 2011, in both the sections, cannot have the effect of altering or effacing the fundamental nature of both the provisions or their respective spheres of operation or to take away the separate identity of section 44BB. We do not, therefore, see how these amendments can assist the Revenue's contention in the present case, put forward by the learned senior standing counsel. We, therefore, agree with the Authority for Advance Rulings that in the present case the profits shall be computed in accordance with the provisions of section 44BB of the Act and not section 44DA."

In the above extracted portion, the court has held that in case the services are in the nature of royalty or fees for technical services so as to fall under section 44DA, then an assessee is rendering such services as provided in section 44BB, he cannot claim the benefit of being assessed on the basis that 10 per cent. of the Revenue will be deemed to be the profits as provided in section 44BB. This legal viewpoint stands reaffirmed and reinforced in *PGS Exploration (Norway) AS* v. *Addl. DIT* (supra).

The upshot of the above discussion is that after April 1, 2011, income falling within the scope of section 44DA(1) of the Act would be excluded 21

from the scope of section 44BB of the Act. If the income of a non-resident is in the nature of fees for technical services or royalty, it shall be taxable under the provisions of either section 44DA or section 115A.

*The definition of fees for technical services and the exception therein*

**22** There is yet another important factor that needs to be illuminated. It is to be borne in mind that as per the *Explanation* to section 44DA, the expression "fees for technical services" shall have the same meaning as in *Explanation 2* to clause (vii) of sub section (1) of section 9. This definition excludes "mining or like projects" from the ambit of the definition of "fees for technical services". The Central Board of Direct Taxes Circular No. 1862, dated October 22, 1990, also clarifies that a rendition of services like training and carrying out drilling operations for exploration/exploitation of oil and natural gas would also be covered within the phrase "mining or like projects" and therefore shall fall outside the ambit of "technical services". The relevant portion of the said circular reads as under :

> "1. The expression 'fees for technical services' has been defined in *Explanation 2* to section 9(1)(vii) of the Income-tax Act, 1961 as under :
>
> *Explanation 2*.—For the purpose of this clause, 'fees for technical services' means any consideration (including any lump sum consideration) for the rendering of any managerial, technical or consultancy services (including the provision of services of technical or other personnel) but does not include consideration for any construction, assembly, mining, or like project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head 'Salaries.'
>
> 2. The question whether prospecting for, or extraction or production of, mineral oil can be termed as 'mining' operations, was referred to the Attorney General of India for his opinion. The Attorney General has opined that such operations are mining operations and the expressions 'mining project' or 'like project' occurring in *Explanation 2* to section 9(1)(vii) of the Income-tax Act would cover rendering of services like imparting of training and carrying out drilling operations for exploration or exploitation of oil and natural gas.
>
> 3. In view of the above opinion, the consideration for such services will not be treated as fees for technical services for the purpose of *Explanation 2* to section 9(1)(vii) of the Income-tax Act, 1961. Payments for such services to a foreign company, therefore, will be income chargeable to tax under the provisions of section 44BB of the

Income-tax Act, 1961 and not under the special provision for the taxation of fees for technical services contained in section 115A, read with section 44D of the Income-tax Act, 1961."

This definition of fees for technical services remains unchanged and Circular No. 1862 dated October 22, 1990 is still in force. Thus, in a nutshell, if the services provided by the assessee constitute services for "mining or like project", the consideration therefor would be excluded from the scope of "fees for technical services". It is well settled that when there are two provisions in an enactment which cannot be reconciled with each other, the doctrine of harmonious construction should be applied and attempt should be to interpret the provisions, if possible, giving effect to both. It is the duty of the courts to avoid "a head on clash" between two sections of the same Act and, "whenever it is possible to do so, to construe provisions which appear to conflict so that they harmonise". It should not be lightly assumed that "Parliament had given with one hand what it took away with the other". The provisions of one section of a statute cannot be used to defeat those of another "unless it is impossible to effect reconciliation between them". Despite the amendments introduced in sections 44BB and 44DA, the Legislature has not amended the definition of fees for technical services and it remains unchanged. It has to be given the meaning that emerges from *Explanation 2*, clause (vii) of sub section (1) of section 9. As a result, if the services are rendered for "mining or like project", the same would not qualify as fees for technical services. Thus, if the income of an assessee is not covered under the definition of fees for technical services, it would get excluded from the purview of section 44DA.

**23** With the above clarity on the legal position, we now proceed to examine the nature of activities performed by the assessee and the income derived therefrom. This is necessary to answer the crucial question in the present case as to whether the receipts from the activities rendered by the assessee fall under section 44BB or fall within the purview of section 44DA after the amendment introduced by the Finance Act, 2010.

*Categorisation of the income of the petitioner : Whether royalty or fees for technical services ?*

*Observations of the Commissioner of Income-tax with regard to categorization of the income of the assessee*

**24** First and foremost, the Commissioner of Income-tax in the impugned order has not returned a categorical finding as to whether the income, or which part of the petitioner's income, falls under royalty and fees for technical services and that has constricted us to conclusively decide the issue

for the reasons explained hereinafter. We are disappointed to note that the Commissioner of Income-tax has not taken any definite stand. The draft assessment order proposed under section 143(3) read with section 143(1) of the Act, held that the income of the assessee has been considered in the nature of royalty/fees for technical services. The assessment was also finalised in the above terms. The petitioner challenged the assessment order by way of a revision under section 264 of the Act where the following ground was urged :

"*Ground No. 1—Claim of section 44BB incorrectly denied.*

On the facts and circumstances of the case, the learned Assessing Officer erred in law and on the facts of the case in holding that the income on account of receipts from provision of software enabled solutions to the oil and gas industry along with providing annual maintenance services of the software is in the nature of fees for technical services/royalty payments under section 9(1)(vii)/9(1)(vi) of the Income-tax Act, 1961 (the 'Act')."

**25** The Commissioner of Income-tax considered the contentions raised by the petitioner and rejected the aforesaid ground inter alia holding as under :

"On a comprehensive consideration of the entire conspectus of the factual matrix of the case and the extant legal position on the issues involved, there is no merit in Ground Nos. 1 and 2 of the assessee, i.e., claim of applicability of section 44BB to the assessee's receipts instead of section 44DA adopted by the Assessing Officer and estimating income at 25 per cent. of the gross revenue/receipts and is therefore rejected. The nature of services rendered are not even wholly connected to drilling and prospecting. The logic of the *ONGC* decision does not apply in this case. In any case, section 44DA adopted by the Assessing Officer and estimating income at 25 per cent. of the gross revenue/receipts and is therefore rejected. The nature of services rendered are not even wholly connected to drilling and prospecting. The logic of the *ONGC* decision does not apply in this case. In any case, the provisions of section 44DA read with amended provisions of section 9(1)(vi) and 9(1)(vii) clearly indicate that the amount should be assessed under section 44DA asroyalty/ fees for technical services. Further, the consistent stand of the Department is that the assessee's income from software licencing and its maintenance is taxable in terms of section 44D/44DA and not under section 44BB of the Income-tax Act, 1961."

From the aforesaid conclusion, it becomes evident that the Commissioner of Income-tax has held that the amount received by the assessee should be assessed under section 44DA as "royalty/fees for technical services". The Commissioner of Income-tax examined the activities performed by the assessee as listed out on the assessee's website and concluded that the assessee is providing software services for processing of raw seismic data. It is noted that the assessee provides software to develop 2D/3D and graphs of the seismic information available and also the maintenance of such software. The Commissioner of Income-tax has concluded that the activities are carried at back end and can be done at any place. On this basis, the Commissioner of Income-tax held that there was no need for the assessee's software at onsite/drilling site and thus since the services provided by the assessee were not directly involved in mining or like operation, the same were not out of the purview of fees for technical services. This is an erroneous approach. It was necessary for the Commissioner of Income-tax to have given a categorical finding as to the nature of receipt in the hands of the assessee. In our considered opinion, the Commissioner of Income-tax fell in error on this aspect. Although, the Commissioner of Income-tax is correct in holding that the "mining or like project" are out of the purview of fees for technical services, and consequently the same would not fall within the ambit of section 44DA(1), however the scope of technical services cannot be broadened by giving a restrictive interpretation to the expression "mining or like project", appearing in *Explanation 2* to clause (vii) of sub section (1) of section 9. The Commissioner of Income-tax perhaps in an attempt to give meaning to the combined effect of the provisions of section 44BB, section 44DA and section 115A has endeavoured to give such an interpretation. However, such a view is flawed, inasmuch as, the scope of expression "mining or like project" has been confined only to situations where services are performed onsite, i.e., at the site of mining/drilling. We are unable to find any rationale in this reasoning. In the impugned order, it has been noted that the software supplied by the petitioner helps to ascertain the drilling spot where there is a maximum probability for finding oil. The impugned order also records that the assessee is regularly hired by Oil and Gas exploration companies such as ONGC, Reliance Industries Ltd., Gujarat State Petroleum Corporations, Oil India Ltd., etc., for availing of the aforesaid services. It has been further noted in para 4.3 (a) that "the services of the assessee prima facie appear to be covered by judgment of the apex court in the case of *ONGC* v. *CIT* (supra), as it is one of the 44 work/activity identified by the court for applying section 44BB instead of section 44D". Reference here may be made to the judgment of the Supreme Court in the case of *ONGC* (supra). In the said case, the court

**26**

applied the doctrine of pith and substance in respect of each contract/ agreement, to ascertain whether the dominant purpose of the agreements was prospecting, extraction or production of mineral oils. On that basis, the court held that the payments made by ONGC and received by non-resident assessees or foreign companies under the contracts is more appropriately assessable under the provisions of section 44BB and not section 44D of the Act. The relevant portion of the said judgment reads as under :

> "The second proviso to sub-section (1) of section 44DA inserted by the Finance Act, 2010, with effect from April 1, 2011 makes the position clear. Simultaneously a reference to section 44DA was inserted in the proviso to sub-section (1) of section 44BB. It should be remembered that section 44DA also requires that the non-resident or the foreign company should carry on business in India through a permanent establishment situated therein and the right, property or contract in respect of which the royalty or fees for technical services is paid should be effectively connected with the permanent establishment. Such a requirement has not been spelt out in section 44BB ; moreover, a flat rate of 10 per cent. of the revenues received by the non-resident for the specific services rendered by it are deemed to be profits from the business chargeable to tax in India under section 44BB, whereas under section 44DA, deduction of expenditure or allowance wholly and exclusively incurred by the non-resident for the business of the permanent establishment in India and for expenditure towards reimbursement of actual expenses by the permanent establishment to its head office or to any of its other offices is allowed from the revenues received by the non-resident. Because of the different modes or methods prescribed in the two sections for computing the profits, it apparently became necessary to clarify the position by making necessary amendments. That perhaps is the reason for inserting the second proviso to sub-section (1) of section 44DA and a reference to section 44DA in the proviso below sub-section (1) of section 44BB. A careful perusal of both the provisos shows that they refer only to computation of the profits under the sections. If both the sections have to be read harmoniously and in such a manner that neither of them becomes a useless lumber then the only way in which the provisos can be given effect to is to understand them as referring only to the computation of profits, and to understand the amendments as having been inserted only to clarify the position. So understood, the proviso to sub-section (1) of section 44BB can only mean that the flat rate of 10 per cent. of the revenues cannot be deemed to be the profits

of the non-resident where the services are of the type which do not fall under that section, but are more general in nature so as to fall under section 44DA. Similarly, the second proviso to sub-section (1) of section 44DA can only be interpreted to mean that where the services are general in nature and fall under the sub-section read with *Explanation 2* to section 9(1)(vii) of the Act, then an assessee rendering such services as provided in section 44BB cannot claim the benefit of being assessed on the basis that 10 per cent. of the revenues will be deemed to be the profits as provided in section 44BB. In other words, the amendment made by the Finance Act, 2010, with effect from April 1, 2011 in both the sections, cannot have the effect of altering or effacing the fundamental nature of both the provisions or their respective spheres of operation or to take away the separate identity of section 44BB. We do not, therefore, see how these amendments can assist the Revenue's contention in the present case, put forward by the learned senior standing counsel. We, therefore, agree with the AAR that in the present case the profits shall be computed in accordance with the provisions of section 44BB of the Act and not section 44DA."

**27** The aforesaid observations of the Supreme Court, where an identical issue was involved, has not been appreciated in the right perspective by the Commissioner of Income-tax. If the nature of services rendered have a proximate nexus with the extraction or production of mineral oils, it would be outside the ambit of the definition of fees for technical services. In the instant case, since the nature of services rendered by the petitioner gets excluded from the definition of "fees for technical services", in the light of what is discussed above, the next logical question that arises for consideration is whether the petitioner can claim the benefit of section 44BB. The answer to this question is contingent on factual determination, as the legal position has changed from April 1, 2011. It is now required to be considered whether the receipts in the hands of the assessee qualify to be "royalty" or not ? If the answer to this question is in the affirmative, then in that event, the relevant provision would now be section 44DA(1).

*The purview of the definition of "Royalty"*

**28** On this aspect, the Commissioner of Income-tax has also made certain observations that the assessee is not transferring the ownership in the software to the purchaser and is only granting a licence to use the same. It has been further held that under clause (v) of *Explanation 2* to section 9(1)(vi) of the Act, transfer of all or any rights in respect of any copyright is "Royalty". It has been held that if the software continues to be owned by

the licensor, the use thereof would amount to "Royalty". The relevant paragraphs (l) and (m) of the impugned order, read as under :

"(I) Under clause (v) of *Explanation 2* to section 9(1)(vi) of the Act, transfer of all or any rights in respect of any copyright is royalty. The term 'in respect of' has been interpreted by the Supreme Court/High Court and given very wide meaning in the following cases :

(i) The Supreme Court in *Shahdara (Delhi) Saharanpur Light Railway Company Ltd.* v. *Upper Doab Sugar Mills Limited* reported in AIR 1960 SC 695, page 695 ;

(ii) The Bombay High Court in *Anusua Vithal* v. *J. H. Mehata, Additional Authority, under Payment of Wages Act*, AIR 1960 Bom 201 ;

(iii) The Patna High Court in *CIT* v. *Chuni Lal Rameshwar Lal* reported in [1968] 70 ITR 167 (Patna) ; AIR 1968 Patna 64.

Relying on these judgments, the Karnataka High Court in the case of *CIT* v. *Synopsis International Old Limited* [2012] 28 taxmann.com 162 (Karn) ; [2013] 212 Taxman 454 (Karn) held that the expression 'in respect of used in *Explanation 2* denotes the intention of Parliament to give a broader meaning and wider connotation that covered all the income from transfer of all or any of the rights in respect of a copyright. The High Court also observed that when the meaning of the words used are clear, unambiguous, merely because it is a fiscal legislation, the meaning cannot be narrowed down and it cannot be interpreted so as to give benefit to the assessee only. Then it would be rewriting the section, under the guise of interpreting a fiscal legislation, which is totally impermissible in law. When the Legislature has advisedly used the words 'in respect of', the intention is clear and manifest, the said phrase being capable of a broader meaning, the same is used in the section to bring within the tax net all the incomes from the transfer of all or any of the rights in respect of a copyright. Thus, it was held that licence fee for use of software amount to transfer of all or any of the rights in respect of a copyright.

(m) When licence is granted to allow use of the software by making copy of the same and to store it in the hard disk of the designated computer and to take back up copy of the software, it is clear that what is transferred is right to use the software, an exclusive right, which the owner of the copyright, i.e., the licensor owns and what is transferred is only right to use copy of the software for the internal business as per the terms and conditions of the agreement. It is also to be noted that what is supplied in such cases is the copy of the soft-

ware of which the respondent-supplier continues to be the owner (and not the end user) and what is granted under the licence is only right to copy the software as per the terms of the agreement, which, but for the licence would amount to infringement of copyright under section 52 of the Copyright Act, 1957. The software continues to be owned by the licensor. On these facts, the use of software will amount to royalty even under the Indian Copyright Act, 1957 and also under Income-tax Act, 1961 in all the 4 categories as given under :

(i) End user of distributors like IBM India Limited, Rational Software Corporation India Limited, Sunrays Computers Private Limited, LG Soft India Pvt. Ltd., M Tech India Private Limited, etc. ; or

(ii) End user of resident supplier of embedded software like Alcatel Lucent India, Microsoft Corpn. India ; or

(iii) End user of non-resident supplier of embedded software like ZTE Corporation, Nokia Network OY, Ericsson ; or

(iv) End user of—non-resident supplier of software—other than embedded software like Citrix Systems Asia Pacific Limited, Synopsis International Limited, etc."

29 Both the sides have referred to several case law in support of their contentions on the plea pertaining to the concept of income from royalty. The petitioner has impugned the decision of the Commissioner of Income-tax, contending that the income from facilities/services of specialized software will not fall within the purview of royalty under section 9(1)(vi) of the Act. The Commissioner of Income-tax has essentially relied upon the judgment of the Karnataka High Court in the case of *CIT* v. *Synopsis International Old Limited* [2012] 28 taxmann.com 162 (Karn) ; [2013] 212 Taxman 454 (Karn) to hold that the expression "in respect of" used in *Explanation 2* denotes the intention of Parliament to give a broader meaning and wider connotation that covers all the income from transfer of all or any of the rights in respect of copyright. The petitioner on the other hand has contended that this court has specifically dissented from the views expressed by the Karnataka High Court. In this regard, reliance has been placed on the decision of this court in *CIT* v. *Alcatel Lucent Canada* [2015] 372 ITR 476 (Delhi) ; *CIT, International Taxation* v. *ZTE Corporation* [2017] 392 ITR 80 (Delhi) ; *DIT* v. *Ericsson A.B.* [2012] 343 ITR 470 (Delhi) and *DIT* v. *Intrasoft Ltd.* [2014] 220 Taxman 273 (Delhi). We need not go into this vexed question at this stage because of lack of clarity on facts.

30 In the assessment order, the Assessing Officer has taken note of the contracts entered into by the petitioner with other parties. A perusal of the same indicates that such contracts are in the nature of annual maintenance contract of upgradation, maintenance in support of software licences ; supply of software ; AMC for software. The nature of activity/scope of services under the contract executed by the petitioner with various companies also indicates the same position. The relevant portion of the order reads as under :

"The nature of activities/scope of work under the contract with various companies is found to be as follows :

(a) Under the contracts/service orders With Calm India Ltd. scope of work includes 'AMC for Paradigm Software' provided by the assessee along with AMC for renewal of Paradigm Software and supply of 'Paradigm Software license'.

(b) Under the contracts/service orders with ONGC Ltd. MAT/IMP/E/2(769)/2009-10 scope of work includes providing service for up-gradation, maintenance and support of Paradigm Interpretation Software provided by the assessee along with AMC for site specific Geolog Paradigm Software at ONGC site in some contracts.

(c) Under ONGC contract 4050006697, the assessee has supplied developed application software along with provision of SKUA software suite licence.

(d) Under ONGC contract MATIIMPIE-I/I2(769)1200iJ-10 and MATIIMPIE-II/2(2772)1201Q-11 awarded by Oil and Natural Gas Corporation Limited for the provision of annual maintenance contract for SKUA Suit of software under corporate licensing.

(e) Under ONGC contract 4050007265 the assessee has supplied CRAM software along with provision of software licence for GEOPIC.

(f) Purchase order number 048fl218157 with Reliance Industries Limited is for supply of perpetual software licence and supply of software to be installed at Reliance facilities in India which comprise of Geolog Software. The assessee also providing software maintenance services along with troubleshooting services and provision of licence key. The assessee is also providing software familiarization support and consultancy services by provision of personnel or providing training, AMC for software is also provided.

(g) Work order number 04813101650 with Reliance Industries Limited is for supply of perpetual software licence and supply of software to be installed at Reliance facilities along with AMC for

maintenance and support services of software in India along with supply of all enhancement and additions to the software.

(h) Service Order number 8300000785 with Gujarat State Petroleum Corporation Ltd. for provision of AMC of Paradigm Software. The assessee is also providing installation and training with respect to the software provided.

(i) Quotation No. US-10-014R2-JS-Q1 ; Quotation No. US-10-014R2-JS-Q2 ; Quotation No. US-10-014R2-JS-Q3 and Quotation No. US-10-014R2-JS-Q4 and with Fugro Geoscience India Pvt. Ltd. for provision of software licence access and support service agreement.

(j) Contract number OIUCCO/GPHY/GLOBAU275110-11 with Oil India Limited for provision of AMC and support services of Paradigm Software. The assessee is also providing services of its engineers who are deputed to site of OIL in India for the contract and maintenance services."

From the above it manifests that the contracts executed by the assessee **31**
are composite contracts and there is no bifurcation with respect to the nature of consideration relating to the services rendered. The assessee has not segregated its activities into supply of software and maintenance/support services. The entire income derived under the contracts was offered for taxation under section 44BB. The Revenue in its note of arguments has contended that "supply of software" is "royalty" and "other services" are "fees for technical services." and accordingly the petitioner is liable to pay tax under section 44DA of the Act. Whether the services of updating the software/renewal of licence or warranty services or maintenance of software are inextricably and essentially linked to the supply of the software and are ancillary services is a question of fact that would require determination after examining the dominant purpose of such contracts. In our opinion, there is no factual clarity on this aspect. We do not find any such distinction/segregation that can be inferred with respect to the receipts in the hands of the assessee under the contracts executed by it, referred above. The Commissioner of Income-tax being a fact-finding body has failed to give a reasoned order with respect to the nature of income and its subsequent application.

*Directions*

In view of the foregoing discussion, we set aside the impugned order **32**
and the matter is remanded to the file of the learned Commissioner of Income-tax to assess the petitioner's income and tax payable thereon by first determining the nature of the income/receipts in the hands of the

assessee in the light of the observations made in this judgment. The Commissioner of Income-tax, would be required to give a finding of fact on the following aspect :

Whether the income from services provided by the assessee including the supply of software as well as ancillary services such as maintenance and installation would be covered under the definition of royalty under the *Explanation 2* to section 9(1)(vi) of the Income-tax Act ?

If the answer to the above question is in the affirmative, the income would be taxable under section 44DA.

On the contrary, if the answer is in the negative, the income of the assessee would not be taxable under section 44DA but section 44BB [as held in *ONGC* (supra) as well as Central Board of Direct Taxes Circular No. 1862, dated October 22, 1990] since it is excluded from the definition of fees for technical services under *Explanation 2* to section 9(1)(vii) of the Act, being covered under the exception relating to mining and like activities provided in the definition of fees for technical services.

Lastly, though this ground has not been raised by the assessee, however, it is required to be examined whether the assessee's case would be covered under the India-Australia Double Taxation Avoidance Agreement. Article 12(3) of the said Double Taxation Avoidance Agreement provides the definition of royalty. The petitioner is granted liberty to claim benefit under the said double taxation avoidance agreement before the learned Commissioner of Income-tax if it wishes to do so. Besides, in the event the answer to the question is in the affirmative, the assessee shall also be at liberty to assail such findings on merit, as we have refrained ourselves from determining whether the income of royalty is excluded from the definition under the Act.

**33** The writ petition is allowed in the above terms.

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**[2020] 424 ITR 561 (Ker)**

[In the Kerala High Court]

# COMMISSIONER OF INCOME-TAX

*v.*

# V. M. VARGHESE AND ANOTHER

**K. Vinod Chandran** and **Ashok Menon** JJ.

May 23, 2018.

**SS ▸ ITA 1961, s 220(2A)**
**HF ▸ Assessee**

Appeal—Delay in filing appeal—Condonation of delay—Abatement of appeal on ground of assessee's death—Delay and laches on part of Department to take up proceedings for setting aside abatement within reasonable time—Delay not explained by Department—Application for condonation of delay rejected—Appeal dismissed as abated—Income-tax Act, 1961, s. 220(2A).

*The Department filed an application to set aside the abatement of appeal by reason of the death of the assessee, condonation of delay of 3345 days, as also impleadment of the legal heir and son of the deceased assessee as additional respondent. The reasons stated in the affidavit to set aside the abatement and condonation of delay were that the Commissioner was not aware of the death of the assessee, that only when the notice issued to the assessee from the court could not be served, was the death of the assessee brought to the notice of the Commissioner and immediately thereafter, the applications were filed :*

Held, *dismissing the application, that it was evident from the communications (the application filed before the Chief Commissioner by the son of the deceased assessee seeking waiver of interest levied under section 220(2A) for the block assessment and the demand dated January 28, 2013 raised on the wife of the assessee by the Tax Recovery Officer giving effect to the Tribunal's order dated October 3, 2002) that the Department was aware of the death of the assessee before the endorsement on the notice issued by the court was received back. The impleading petition was filed only on August 3, 2016. In the year 2013, the Tax Recovery Officer had implemented the order of the Tribunal and had communicated the demand to the wife of the deceased assessee. Before giving effect to the order, the Tax Recovery Officer should have enquired about the further proceedings taken on the basis of the order of the Tribunal and this appeal itself was filed in the year 2003. Notice was issued only in the year 2009. The Department ought to have taken up the proceedings for setting aside the abatement and condonation of delay within*

*a reasonable period and there was no explanation for the gross delay caused. Hence the applications were to be rejected.*

**I. T. A. No. 1429 of 2009.**

*P. K. R. Menon*, Senior Counsel, Government of India (Taxes) and *Jose Joseph*, Standing Counsel, for Income-tax Department, for the appellant.

*M. Gopikrishnan Nambiar*, *P. Gopinath*, *P. Benny Thomas*, *K. John Mathai*, *Joson Manavalan* and *Kuryan Thomas*, Advocates, for the respondents.

**JUDGMENT**

The judgment of the court was delivered by

1 K. VINOD CHANDRAN J.—The preliminary question raised is whether the appeal has to be heard on the merits since by reason of the death of the assessee, there is abatement of the above appeal. The Revenue has filed an application for setting aside the abatement, condonation of delay of 3345 days, as also impleading the counter-petitioner, the legal heir of the assessee as additional respondent. The additional respondent now sought to be impleaded is the son of the deceased assessee. The reasons stated in the affidavit accompanying the application for setting aside the abatement and condonation of delay are that the appellant-Commissioner of Income-tax, Kochi was not aware of the death of the respondent. Only when the notice issued to the respondent from this court could not be served, the death of the respondent-assessee was brought to the notice of the Commissioner and immediately thereafter, the aforesaid applications were filed.

2 A counter-affidavit has been filed by the son of the assessee, who is sought to be impleaded. Annexure R(1)(a) is an application filed before the Chief Commissioner of Income-tax, Kochi by the son of the deceased seeking waiver of interest levied under section 220(2A) for the block assessment, which is dated February 2, 2011. Annexure R(1)(b) is a letter addressed by the Tax Recovery Officer specifically raising a demand on giving effect to the Tribunal's order dated October 3, 2002, which is challenged in the above appeal. The said demand is dated January 28, 2013. The demand has been raised on the wife of the assessee, showing the assessee as deceased. These communications make it clear that the Department was aware of the death of the assessee long before the endorsement on notice issued by this court was received back. The impleading petition is filed only on August 3, 2016.

3 The learned standing counsel for the Revenue submits that the appeal is filed by the Commissioner of Income-tax, Kochi and the annexures

produced along with the counter-affidavit are with respect to different officers. We are of the opinion that the Revenue cannot take such a contention, especially in the context of Tax Recovery Officer having sent a communication to the wife of the deceased-assessee specifically giving effect to the order of the Income-tax Appellate Tribunal, which is challenged here. The Tax Recovery Officer would necessarily have, before giving effect to the order, enquired about the further proceedings taken on the basis of the order of the Income-tax Appellate Tribunal and this appeal itself was filed in the year 2003. Notice was issued only in the year 2009 for reason of the appeals having not been numbered for reason of the challenge raised to the court fees applicable by way of amendment of the Kerala Court Fees and Suits Valuation Act. However, the appeals were filed in time and was pending before this court unnumbered till 2009 and thereafter numbered. In the year 2013, the Tax Recovery Officer has implemented the order and had communicated the demand to the wife of the deceased assessee. The Department ought to have taken up the proceedings for setting aside the abatement and condonation of delay, if at all, within a reasonable period from annexure R(1)(a) or R(1)(b). We do not see any explanation for the gross delay caused. The applications hence would stand rejected and as a consequence, the appeal is dismissed as abated, leaving the question of law to be considered in appropriate proceedings.

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**[2020] 424 ITR 563 (Bom)**

[In the Bombay High Court]

## PRINCIPAL COMMISSIONER OF INCOME-TAX

*v.*

## EIGHT ROADS INVESTMENT ADVISORS PVT. LTD.

**Ujjal Bhuyan** and **Milind N. Jadhav** JJ.

February 27, 2020.

**SS ▸ ITA 1961, ss 92CA, 260A**
**AY ▸ 2010-11**
**HF ▸ Assessee**

International transactions—Appeal to High Court—Determination of arm's length price—Order of Tribunal based on facts—No question of law arose—Income-ax Act, 1961, ss. 92CA, 260A.

*Section 92 of the Income-tax Act, 1961, deals with computation of income from international transactions at arm's length price. Section 92A defines an associated enterprise in relation to another enterprise. Section 92CA deals with reference to a Transfer Pricing Officer. Rules 10A, 10AB, 10B, 10C and 10CA of the Income-tax Rules, 1962 prescribe the manner for working out the arm's length price under the prescribed methods. From the scheme of assessment, it is clear that the process of determination of the arm's length price has to be undertaken by the expert wing of the Income-tax Department which is manned by the Transfer Pricing Officer and at the higher level by a collegium of three Commissioners in the form of the Dispute Resolution Panel whose orders are appealable before the Appellate Tribunal. The exercise to arrive at the arm's length price which is essentially a matter of estimate of the fair value which the Indian company had paid to or had received from its associated enterprise is required to be undertaken by the Transfer Pricing Officer on the basis of the facts and figures relating to comparable cases of other similarly placed entities, whose relevant data is available in the public domain. Under the provisions of the Act and the Rules, the assessee-company is required to furnish its own transfer pricing analysis and the list of chosen comparables which may or may not be agreed to by the Revenue authorities. The entire exercise of making transfer pricing adjustments on the basis of comparables is nothing but a matter of estimate of a broad and fair guess-work of the authorities based on factual relevant materials brought before the authorities, i. e., the Transfer Pricing Officer, the Dispute Resolution Panel and the Appellate Tribunal, which are the fact finding authorities.*

*The entry into the High Court under section 260A of the Act is locked with the words "substantial questions of law" and the key to open that lock to maintain such appeal can only be the perversity of the findings of the Tribunal in these type of cases and the perversity in the findings not only averred by the appellant before the court but established on the basis of cogent material which was available before the authorities below including the Tribunal. The findings arrived at by the Tribunal can be held to be perverse within the well settled parameters for determining them as perverse. It is not open to either of the parties, i. e., the assessee or the Department to invoke the jurisdiction of the court under section 260A of the Act merely because the Tribunal comes to reverse or modify the findings given by the lower authority, viz., the Transfer Pricing Officer ) or the Dispute Resolution Panel.*

*The assessee-company filed its return of income declaring a total income of Rs. 7,00,51,101 for the assessment year 2010-11. The case of the assessee was*

*selected for scrutiny and statutory notice under section 143(2) was issued, also notice under section 142(1), inter alia, calling for various details in connection with the scrutiny assessment proceedings. The assessee-company through its authorised representative furnished the details called for. Thereafter the Assessing Officer discussed the case. Reference was made to the Transfer Pricing Officer for computation of the arm's length price in relation to the international transactions. The Transfer Pricing Officer by his draft order reported an upward adjustment of Rs. 4,96,42,540 of the arm's length price of the international transactions made by the assessee with its associated enterprises. The assessee was given a fair chance to explain why the transfer pricing adjustment of Rs. 4,96,42,540 should not be made. The Transfer Pricing Officer after hearing the assessee passed an order under section 92CA(iii) making an upward adjustment of Rs. 4,96,42,540. The assessee filed its objections against the order of the Transfer Pricing Officer before the Dispute Resolution Panel. The Dispute Resolution Panel held that the draft order passed by the Transfer Pricing Officer was sustainable and did not require any interference. The assessee approached the Tribunal against the order of the Dispute Resolution Panel. The Tribunal after a thorough analysis of each comparable offered reasons for inclusion of the six comparables which were excluded by the Transfer Pricing Officer and the Dispute Resolution Panel. The Tribunal directed the Assessing Officer/Transfer Pricing Officer to determine the arm's length price afresh in terms of the directions contained in the order. On appeal :*

Held, *dismissing the appeal, that the Tribunal had considered the case of each comparable company and discussed the parameters of the comparables for the purposes of including or excluding them as comparables on the basis of the functionality of the companies in the public domain. Such a detailed exercise having been undertaken by the Tribunal qua each and every comparable company, the reasons given by the Tribunal could not be faulted in respect of the comparable companies. The findings arrived at by the Tribunal were entirely findings of fact and the Revenue had failed to show any perversity in the order. The order of the Tribunal was valid and no question of law arose from it.*

Cases referred to :

Carlyle India Advisors Pvt. Ltd. *v.* Deputy CIT [2014] 43 taxmann.com 184 (Mumbai-(Trib)) (para 11)

CIT (Pr.) *v.* Bain Capital and Advisors (I) P. Ltd. (Income Tax Appeal No. 541 of 2016, dated 24-11-2018) (para 18)

CIT *v.* Carlyle India Advisors Pvt. Ltd. [2013] 357 ITR 584 (Bom) (para 5)

CIT (Pr.) *v.* Softbrands India Pvt. Ltd. [2018] 406 ITR 513 (Karn) (para 10)

CIT (Pr.) *v.* Temasek Holdings Advisors India Pvt. Ltd. (Income Tax Appeal No. 304 of 2017, dated 16-4-2019) (para 16)

CIT (Pr.) *v.* WSP Consultants India Pvt. Ltd. [2018] 253 Taxman 58 (Delhi) ; [2017] 87 taxmann.com 266 (Delhi) (para 8)

General Atlantic Pvt. Ltd. *v.* Asst. CIT [2013] 25 ITR (Trib) 389 (Mumbai) (para 5)

Goldman Sachs India Securities Pvt. Ltd. *v.* CIT [2016] 69 taxmann.com 19 (Bom) (para 5)

Trilogy E-Business Software India P. Ltd. *v.* Deputy CIT [2013] 23 ITR (Trib) 464 (Bang) (para 11)

**Income Tax Appeal No. 1125 of 2017.**

*A. R. Malhotra,* along with *N. A. Kazi,* Advocates, for the appellant.

*Nishant Thakkar,* along with *Ms. Jasmin Amalsadwala* instructed by *PDS Legal*, Advocates, for the respondent.

**JUDGMENT**

The judgment of the court was delivered by

1 MILIND N. JADHAV J.—This appeal has been preferred under section 260A of the Income-tax Act, 1961 (for short "the said Act") for the assessment year 2010-11, against the order dated October 25, 2016 passed by the Income-tax Appellate Tribunal "K" Bench, Mumbai (hereinafter referred to as "Tribunal").

2 The respondent-assessee entered into an international transaction of non-binding investment advisory services with its associated enterprises (for short "A.E.") and earned revenue of Rs. 25.83 crores during the assessment year 2010-11. The assessee for the purpose of bench marking the transaction adopted transactional net margin method (for short "TNMM") as an appropriate method under the provisions of section 92C of the Act and identified seven comparable companies as comparables with their three years average weighted margin of 18.23 per cent. and operating margin being at 19.67 per cent. for the purpose of claiming the international transaction to be at arm's length.

2.1 The Assessing Officer (for short "AO") framed a draft assessment order dated February 26, 2014 making an upward revision of transfer pricing adjustment of Rs. 4,96,42,540. The assessee approached the Dispute Resolution Panel (for short "DRP") against the draft assessment order with

its objections. The Dispute Resolution Panel vide order dated October 7, 2014 rejected the contentions and objections raised by the assessee in relation to upward revision of transfer pricing adjustment and directed the Assessing Officer to finalise the draft assessment, resulting in passing of the impugned assessment order. The Assessing Officer/Transfer Pricing Officer (for short "Transfer Pricing Officer") by his final order dated October 31, 2014 rejected the transfer pricing study of the assessee on the basis of various defects and deficiencies and rejected six out of seven comparables selected by the assessee while retaining one comparable on the basis of single year data. However in the said order the Transfer Pricing Officer proceeded and selected six new comparable companies as comparables with an arithmetic mean of 42.66 per cent. of operating margin. The Transfer Pricing Officer applied the aforesaid arithmetic mean to be operating cost of the assessee and determined the arm's length price of Rs. 30,79,92,412 as against the international transaction price of Rs. 25,83,49,872 resulting in a short fall of Rs. 4,96,42,540. This short fall was treated as transfer pricing by the Transfer Pricing Officer.

The above order was assailed by the assessee before the Tribunal. The **3** Tribunal by the impugned order dated October 25, 2016 allowed the appeal filed by the assessee in elaborate detail with respect to selection of each comparable company by the Transfer Pricing Officer and Dispute Resolution Panel and directed the Assessing Officer/Transfer Pricing Officer to determine the arm's length price afresh in terms of fresh directions given by the Tribunal in respect of each comparable company. Being aggrieved by the order passed by the Tribunal the Revenue is in appeal before us.

The Revenue has projected the following substantial questions of law : **4**

"6.1 Whether on the facts and circumstances of the case and in law, the hon'ble Income-tax Appellate Tribunal was justified in directing to exclude for functionally comparable companies from the list of comparables selected by the Transfer Pricing Officer, viz. M/s. IDFC Investment Advisors Pvt. Ltd., M/s. ICRA Online Ltd., M/s. Motilal Oswal Investment Advisors Pvt. Ltd. and M/s. Kshitij Investment Advisory Co. Ltd., on the ground of functional dissimilarity ?

6.2 Whether on the facts and circumstances of the case and in law, the hon'ble Income-tax Appellate Tribunal was justified in directing to consider four companies, viz., M/s. ICRA Management Consulting Services Pvt. Ltd., M/s. IDC India Limited, M/s. Informed Technology Ltd. and M/s. Kinetic Trust Ltd. as comparable even though

these companies are not functionally comparable to that of the assessee ?

6.3 Whether on the facts and circumstances of the case and in law, the hon'ble Income-tax Appellate Tribunal was justified in directing not to consider M/s. IDFC Investment Advisors Ltd. as a comparable, without appreciating the fact that the said company has earned Rs. 13.42 crores from investment advisory services out of total revenue of Rs. 26.29 crores ?

6.4 Whether on the facts and circumstances of the case and in law, the hon'ble Income-tax Appellate Tribunal was justified in directing not to consider M/s. ICRA Online Ltd. as a comparable without appreciating the fact that the Transfer Pricing Officer has used segmental results of 'outsourced services' of the said company for comparative purpose and that segment is functionally similar to that of the assessee ?

6.5 Whether on the facts and circumstances of the case and in law, the hon'ble Income-tax Appellate Tribunal was justified in directing not to consider M/s. Motilal Oswal Investment Advisors Pvt. Ltd. as a comparable without appreciating the fresh facts brought on record by the Transfer Pricing Officer in respect of functions performed and assets employed by the said company under section 133 (6) such as employee profile and income received from top clients of the said company ?

6.6 Whether on the facts and in the circumstances of the case and in law, the hon'ble Income-tax Appellate Tribunal was justified in directing not to consider M/s. Kshitij Investment Advisory Co. Ltd. as a comparable on account of peculiar economic circumstances arising as a result of realignment with another company, simply relying on the decision of the hon'ble Income-tax Appellate Tribunal in the case of *Carlyle India Advisors Pvt. Ltd.* , I. T. A. No. 1040/Mum/2015 and *AGM Advisors India Pvt. Ltd.,* I. T. A. No. 4757/Mum/2015, without appreciating the fact that the realignment has not resulted in any change of activity of the business of the said company ?

6.7 Whether on the facts and in the circumstances of the case and in law, the hon'ble Income-tax Appellate Tribunal was justified in directing not to consider M/s. Kshitij Investment Advisory Co. Ltd. as a comparable without appreciating the fresh facts brought on record by the Transfer Pricing Officer in respect of functions performed and

assets employed by the said company under section 133(6) such as employee profile and income received from top clients of the said company ?

6.8 Whether on the facts and circumstances of the case and in law, the hon'ble Income-tax Appellate Tribunal was justified in directing to consider M/s. ICRA Management Consulting Services Pvt. Ltd. as a comparable without appreciating the fact that the said company is not into investment advisory services and the assessee-company has also itself submitted in the course of TP proceedings that the functions performed by this company are not exactly similar to the assessee-company ?

6.9 Whether on the facts and circumstances of the case and in law, the hon'ble Income-tax Appellate Tribunal was justified in directing to consider M/s. ICRA Management Consulting Services Pvt. Ltd. as a comparable without appreciating the fresh facts brought on record by the Transfer Pricing Officer in respect of functions performed and assets employed by the said company under section 133(6) to substantiate that the services provided to top ten clients of the said companies and its employee profile are different from that of the assessee during the year under consideration ?

6.10 Whether on the facts and circumstances of the case and in law, the hon'ble Income-tax Appellate Tribunal was justified in directing to consider M/s. IDC India Ltd. as a comparable without appreciating the fact that the said company is not into investment advisory services and the assessee-company has also itself submitted in the course of TP proceedings that the functions performed by this company are not exactly similar to the assessee-company ?

6.11 Whether on the facts and circumstances of the case and in law, the hon'ble Income-tax Appellate Tribunal was justified in directing to consider M/s. Informed Technology Ltd. as a comparable without appreciating the fact that the said company is not into investment advisory services and the assessee-company has also itself submitted in the course of TP proceedings that the functions performed by this company are not exactly similar to the assessee-company ?

6.12 Whether on the facts and circumstances of the case and in law, the hon'ble Income-tax Appellate Tribunal was justified in directing to consider M/s. Kinetic Trust Ltd. as a comparable without

appreciating the fact that the said company is not into investment advisory services and its turnover is less than Rs. 1 crore ?"

5 We may now advert to the relevant facts necessary for appreciating the controversy in question :

5.1. The assessee-company filed return of income on October 11, 2010 declaring a total income of Rs. 7,00,51,101 for the assessment year 2010-11. The case of the assessee was selected for scrutiny and statutory notice under section 143(2) of the Act was issued, also notice under section 142(1), inter alia, calling for various details in connection with scrutiny assessment proceedings. The assessee-company through its authorised representative furnished the details called for. Thereafter the Assessing Officer discussed the case. Reference was made to the Transfer Pricing Officer for computation of arm's length price in relation to the international transaction. The Transfer Pricing Officer by his draft order dated February 26, 2014 reported an upward adjustment of Rs. 4,96,42,540 in respect of the value of the international transaction made by the assessee with its associated enterprises with regard to the arm's length price. The assessee was given a fair chance to explain as to why the addition should not be made on the transfer pricing adjustment of Rs. 4,96,42,540. The Transfer Pricing Officer after hearing the assessee passed an order under section 92CA(iii) of the said Act making an upward adjustment to the tune of Rs. 4,96,42,540.

5.2. The assessee chose the following seven comparable companies for the purposes of bench marking :-

| *S. No.* | *Name of the company* |
|---|---|
| 1 | Access India Advisors Limited |
| 2 | Future Capital Investment Advisors Limited |
| 3 | ICRA Management Consulting Services Limited |
| 4 | IDC (India) Limited |
| 5 | Informed Technologies Limited |
| 6 | Integrated Capital Services Limited |
| 7 | Kinetic Trust Limited |

The Transfer Pricing Officer after considering various aspects of the comparable companies rejected six out of the aforesaid seven comparables chosen by the assessee. The Transfer Pricing Officer accepted only one company which was Future Capital Investment Advisors Limited and after undertaking a further detailed analysis of the entire matrix of acceptance

and rejection based on profit and operating margin proposed to include five fresh/new comparables as under :-

| *S. No.* | *Name of the company* |
|---|---|
| 1 | Future Capital Holdings Limited (Segmental) |
| 2 | ICRA Online Limited (Segmental) |
| 3 | IDFC Investment Advisors Private Limited |
| 4 | Kshitij Investment Advisors Limited |
| 5 | Motilal Oswal Investment Advisors Private Limited |

The Transfer Pricing Officer included the above five comparable companies in the set of comparables and thus finalised a set of six comparables for the purpose of bench marking the international transaction of the assessee. The Transfer Pricing Officer considered the financial data and annual reports of the six comparables for the financial year 2009-10 as per rule 10B(4) and with the arithmetic mean of their operating margin being at 42.66 per cent. arrived at an upward adjustment of Rs. 4,96,42,540 in his order.

5.3. The assessee filed its objection against the order of Transfer Pricing Officer before the Dispute Resolution Panel, III, Mumbai. Before the Dispute Resolution Panel the assessee summarised that it had entered into an international transaction with its associated enterprises to provide investment advisory services of Rs. 25.83 crores. The assessee for the purpose of bench marking the international transaction had chosen the transactional net margin method as the most appropriate method and identified seven comparable companies with their three years average weighted margin of 18.23 per cent. and operating profit margin being 19.67 per cent., for providing investment advisory services to be at arm's length.

5.4. The Dispute Resolution Panel considered the submissions of the assessee citing functional details as also related party transactions in the case of comparables which were rejected by the Transfer Pricing Officer and returned a finding that for the reasons given by the Transfer Pricing Officer in his draft order which were in substantial detail regarding non-submission of financials and other details of the associated enterprises, rejected the comparables adopted by the assessee and included the new comparables suggested by the Transfer Pricing Officer. Dispute Resolution Panel held that draft order passed by the Transfer Pricing Officer was sustainable and did not require any interference in the bench marking done by the Transfer Pricing Officer. Accordingly, the Assessing Officer vide his

final order dated October 31, 2014 completed the assessment in terms of order dated October 7, 2014 passed by the Dispute Resolution Panel (DRP)–III, Mumbai.

5.5. The assessee approached the Tribunal against the order of the Dispute Resolution Panel. The Tribunal after a thorough analysis of each comparable offered the following reasons for inclusion of the six rejected comparables which were excluded by the Transfer Pricing Officer and Dispute Resolution Panel. For the sake of completeness, we would like to delve into the scrutiny and reasons given by the Tribunal in respect of each of the comparables which came to be included by the Tribunal as comparables.

*New comparables selected by the Transfer Pricing Officer/Dispute Resolution Panel which were rejected by the Tribunal*

5.6 *IDFC Investment Advisors Pvt. Ltd.*

Before the Tribunal the assessee objected to the selection of this company as a comparable by the Transfer Pricing Officer on the ground that the said company was primarily engaged in providing portfolio management services (PMS). The assessee submitted that portfolio management services and investment banking services were functionally different from investment advisory services undertaken by the assessee. The assessee-company was an investment advisory service company as stated in its annual report in relation to IDFC which was actually a portfolio management services. The assessee submitted that, functions performed by this company such as investment and brokerage were performed by an Investment Advisor (IA). After a detailed scrutiny of the profit and loss account of this company, it was revealed that this company was engaged in a number of activities as reported by the Revenue under one segment. Unlike the assessee, the functions performed, assets employed and risks undertaken by this company were totally different from the functions performed by the assessee-company. Therefore it could not be treated as a comparable. In support of the above propositions to challenge the inclusion of IDFC Investment Advisors Pvt. Ltd. as comparable by the Transfer Pricing Officer/Dispute Resolution Panel, the assessee relied upon the following judgments.

"(i) *AGM India Advisors Pvt. Ltd.* v. *Deputy CIT* I. T. A. No. 4757/Mum./2015, the assessment year 2010-11, order dated May 18, 2016 ;

(ii) *Carlyle India Advisors Pvt. Ltd.* I. T. A. No. 1040/Mum./2015, the assessment year 2010-11, order dated November 18, 2015 ;

(iii) *Bain Capital Advisors (India) Pvt. Ltd.* v. *Deputy CIT* I. T. A. No. 413/Mum./2015, the assessment year 2010-11, order dated May 15, 2015 ;

(iv) *Sparkles Dhandho Advisors P. Ltd.* v. *ITO* I. T. A. No. 1047/Mum./2015, order dated December 31, 2015 ;

(v) *CIT* v. *Carlyle India Advisors Pvt. Ltd.* [2013] 357 ITR 584 (Bom) ; [2013] 32 taxmann.com 23, assessment year 2007-08 ;

(vi) *General Atlantic Pvt. Ltd.* v. *Asst. CIT* [2013] 25 ITR (Trib) 389 (Mumbai) I. T. A. No. 7638/Mum./2011 order dated May 17, 2013 ;

(vii) *Goldman Sachs India Securities Pvt. Ltd.* v. *CIT* [2016] 69 taxmann.com 19 (Bom)."

The Tribunal after considering the submissions and more specifically findings expressed by the Tribunal, Mumbai Bench in the case of *AGM India Advisors Pvt. Ltd.* (supra) concluded that as seen in the case of *Carlyle India Advisors Pvt. Ltd.* (supra) after perusing the annual report of this company, the Tribunal had arrived at a finding that the said company was engaged in providing portfolio management services and such services were fee based and the said company had earned revenue from different segments such as portfolio management fee, performance fee, advisory fee etc. On this basis, the Tribunal arrived at a finding that in the above scenario, where a company was remunerated on cost plus basis, it was risk insulated and therefore, on application of FAR analysis, it could be compared with other companies if there is any difference in its functions. The Tribunal referred to the observation of the hon'ble High Court in the case of *General Atlantic Pvt Ltd.* (supra) while approving the view expressed in *Carlyle India Advisors Pvt. Ltd.* (supra), rejected this company, i.e., IDFC Investment Advisors Pvt. Ltd as a comparable.

*5.7 ICRA Online Limited (Segmental)*

The assessee objected to the selection of this company as a comparable selected by the Transfer Pricing Officer as this company had three lines of business verticals, viz., outsource service, information service and software products/service. The assessee submitted that the financials of this company did not indicate the kind of service rendered by the outsource service segment and its annual report was silent thereon. The assessee submitted that information provided on the web site of this company showed that it had two strategic lines of business namely knowledge process outsourcing (KPO) and information service and technology solutions. The assessee submitted that performance of the aforesaid activities made this company financially different from the assessee and hence, it could in no way be

treated as comparable with the assessee-company. The Tribunal on a perusal of the information submitted in the annual report of this company as well as its financials, returned a finding that the functions undertaken by this company were totally different from the assessee-company and therefore the company failed in the FAR analysis itself. Thus, the Tribunal rejected this company, i.e., ICRA Online Limited (Segmental) as a comparable.

*5.8 Motilal Oswal Investment Advisors Pvt. Ltd. (MOIAPL)*

The assessee objected to this company as a comparable selected by the Transfer Pricing Officer as it derived its business verticals from equity capital market, mergers and acquisition, private equity syndication and structural debts. The assessee submitted that as per this company's annual report, the company advised Indian Corporates on cross border acquisitions and this company was a SEBI regulated merchant banker which provided investment banking services in the nature of acquisition equity placements, initial public offers, syndication, etc. and had undertaken activities as lead manager/arranger/sole book runner etc. for various portfolios and earned investment banking fee for the same. The assessee therefore submitted that, this company was not comparable to a non-binding investment advisory and related service provider like the assessee. The Tribunal after going through the annual report of this company returned a finding that, this company was functionally different from the assessee because of the functions performed, assets employed and risk undertaken and failed in the FAR analysis. Thus, the Tribunal rejected this company, i.e., MOIAPL as a comparable.

*5.9 Kshitij Investment Advisory Company Limited*

The assessee objected to this company as a comparable selected by the Transfer Pricing Officer as this company had entered into an agreement with another company, namely, Everstone Investment Advisors Pvt. Ltd. to realign its investment advisory activities with effect from January 1, 2010 and as a result of such joint venture, its entire business was restructured. The assessee submitted that, the profit and loss account of this company for the financial year 2010-11 revealed that no revenue was earned from investment advisory business. The assessee submitted that this company had operated only for nine months during the financial year 2009-10 and hence could not be compared to the assessee. The Tribunal after considering the material available on record and the decisions in *Carlyle India Advisors Pvt. Ltd.* (supra) followed by *AGM India Advisors Pvt. Ltd.* (supra) returned a finding that this company could not be treated as a comparable. The Tribunal based its finding on the decisions given in the afore-

said two cases, in respect of this company pertaining to the very same assessment year and followed the decisions of the Co-ordinate Bench in excluding this company from the list of comparables.

The assessee had suggested the following companies as comparables 6
which were originally rejected by the Transfer Pricing Officer/Dispute Resolution Panel, but were accepted by the Tribunal as comparables after a detailed scrutiny.

*6.1 ICRA Management Consulting Service Pvt. Ltd.*

This company was rejected by the Transfer Pricing Officer/Dispute Resolution Panel as a comparable. This company offered consulting/advisory services through different business groups and practice areas pertaining to strategy, risk management, operations improvement, corporate advisory etc. On the basis of the profit and loss account statement of this company, the assessee submitted that this company derived its revenue from consulting fees. It was the assessee's case that the functions performed by this company with respect to management consultancy service involved analysis of business and operations of a company, its profitability, operational efficiency, future outlook, etc. based on which consultancy or advise is given to the management of a company. Such functions were similar to that of a non-binding investment advisory and related services rendered by the assessee. The assessee submitted that this company had undertaken activities in other fields like business and operations, geographic research discussing the regulations laid out in the bio-generics globally, market research in respect of various products, business and operation analysis and therefore, this company ought to have been accepted as a comparable in the assessee's own case by the Transfer Pricing Officer/Dispute Resolution Panel. The case of the Departmental representative was that this company operated in various verticals as also conducted its business through various practice divisions such as Government and infrastructure practice, energy practice, banking and financial service, corporate advisor practice etc. The assessee however on the basis of documentary evidence which were placed on record submitted that the service provided by this company covered a wide spectrum of activities which were essentially advisory service. Hence, this company could be determined as a comparable. The Tribunal considered these submissions and in view of the above, following the decisions of the Co-ordinate Bench in the case of *AGM India Advisors Pvt. Ltd.* (supra) and in the decision of *Temasek Holdings Advisors India Pvt. Ltd.* (supra) included this company as a comparable.

*6.2 IDC India Limited*

This company was rejected by the Transfer Pricing Officer/Dispute Resolution Panel as a comparable. This company was engaged in the business of research and certificate globally, it was provider of market intelligence advisory services and events for information technology, telecom and consumer technology markets. The assessee submitted that, this company was engaged in research and survey functions which were functionally comparable to advisory support services rendered by the assessee. The assessee submitted that, in the assessee's own case for the assessment year 2009-10, this company had been accepted as a comparable by the Transfer Pricing Officer/Dispute Resolution Panel and therefore there was no reason to exclude the same in the related assessment year. The Tribunal after considering the materials available on record with reference to this company rejected the submission of the Departmental representative for exclusion, by referring to a similar submission made by the Department in the case of *Temasek Holdings Advisors India Pvt. Ltd.* (supra) and relying upon the Co-ordinate Bench decision in the case of *AGM India Advisors Pvt. Ltd.* (supra) included this company as comparable.

*6.3 Informed Technologies Limited*

This company was rejected by the Transfer Pricing Officer/Dispute Resolution Panel as a comparable. This company collected and analysed data on financial fundamentals, corporate governance, director/executive compensation and capital market and this was similar to work done by the assessee who was involved in data analysis of potential clients, analyzing market conditions, conducting research in various sectors, markets, companies etc. After perusal of the annual report of the company and relying on the decisions passed in the case of *Temasek Holdings Advisors India Pvt. Ltd.* (supra), the Tribunal held that since the Transfer Pricing Officer/Dispute Resolution Panel had accepted it as a comparable in the assessee's own case for the assessment year 2009-10, this company should not be excluded from the list of comparables.

*6.4 Kinetic Trust Limited*

This company was rejected by the Transfer Pricing Officer/Dispute Resolution Panel as a comparable. On the basis of annual report of this company, the fact of this company was accepted as a comparable to the assessee by the Transfer Pricing Officer/Dispute Resolution Panel for the assessment year 2009-10 was considered by the Tribunal. Referring to the decision of *Temasek Holdings Advisors India Pvt. Ltd.* (supra), as also the decision of the Tribunal, Delhi Bench, in *Nortel Network India Pvt. Ltd.* (supra) which was affirmed by the Delhi High Court in *Nortel Network*

*India Pvt. Ltd.*, I. T. A. No. 3043/2015, the issue of application of "Turnover filter" was analysed and the Tribunal concluded that if this company was functionally similar, only because of low turnover filter it could not be rejected. The Tribunal included this company as a comparable.

6.5 The Tribunal by the impugned order directed the Assessing Officer/Transfer Pricing Officer to determine the arm's length price afresh in terms of the directions contained in the order.

We have perused and considered the draft assessment order dated February 26, 2014, the assessment order under section 143(3) of the Act dated October 31, 2014, the Dispute Resolution Panel order under section 144C(1) of the Act dated October 7, 2014, and the Tribunal's order dated October 25, 2016 with the assistance of Shri Malhotra and Shri Thakkar appearing on behalf of the respective parties. 7

At the outset, we would like to state that, the findings arrived at by the Tribunal are entirely one of facts and the Revenue has failed to show as to how the said findings are perverse in any manner whatsoever. The Delhi High Court in *Pr. CIT* v. *WSP Consultants India Pvt. Ltd.* reported [2018] 253 Taxman 58 (Delhi) ; [2017] 87 taxmann.com 266 (Delhi) observed thus : 8

> "10. Any inclusion or exclusion of comparables per se cannot be treated as a question of law unless it is demonstrated to the court that the Tribunal or any other lower authority took into account irrelevant consideration or excluded relevant factors in the ALP determination that impact significantly."

Though the Revenue says that the questions projected in paragraph Nos. 6.1 to 6.12 are not just questions of law but substantial questions of law, the assessee disagrees with the same and submits that the Tribunal's order has been rendered on purely factual questions which are consistent with the materials placed on record and hence, in the submission of the assessee, the appeal deserves to be dismissed.

We would state that before the Tribunal one of the principal submissions was that in the assessee's own case similar questions had been dealt with for the previous assessment year in respect of the same comparable and therefore, heavy reliance was placed on the earlier order of the Tribunal in the assessee's own case for accepting the comparables (which were excluded in the present year). 9

At this stage, we would like to refer to the judgment passed by the Karnataka High Court in I. T. A. No. 536 of 2015 along with I. T. A. No. 537 of 2015, in the case of *Pr. CIT* v. *Softbrands India Pvt. Ltd.* [2018] 406 ITR 513 (Karn) delivered on June 25, 2018, which has been relied upon by the 10

assessee. The special provisions relating to avoidance of tax in Chapter X of the Act comprising of sections 92 to 94B with regard to assessment to be done for computation of income from international transactions on the principles of arm's length price and perspective of international trade and transactions are enumerated in paragraph Nos. 3 to 6 therein which read thus (page 516 of 406 ITR) :

"The Indian Income-tax Act, 1961 contains special provisions relating to avoidance of tax in Chapter X of the Act comprising of sections 92 to 94B with regard to assessment to be done for computation of income from international transactions on the principles of 'arm's length price' (ALP) and the relevant Rules for computation of such income under the aforesaid provisions of Chapter X are enacted in the form of rules 10A to 10E in the Income-tax Rules, 1962.

*Perspective of international trade and transactions* :

With the ever increasing international trade and transactions, particularly, in the software Industries and Bangalore, being the silicon valley of India where many big, small and medium size software industries have their offices and units in this software industry, and Bengaluru is a hub of this service industry and essentially the Indian companies have business linkages with large companies spread worldwide particularly in the Western Hemisphere of the globe.

The implementation of the tax laws in this field in a smooth, clear and quick manner is of utmost importance to build an image of an efficient tax administration both at Departmental level and in judicial courts so that the economic activity in such borderless trade thrives and enures to the benefit of the Indian economy at large and software industry in particular.

While the special provisions have been made for computation of 'arm's length price' to arrive at a fair assessment of income taxable in the hands of the Indian resident companies and these special provisions also provide for an elaborate and in-depth analysis of huge data of the comparable cases of other similarly situated companies to arrive at a fair 'arm's length price' and for that, special cells and designated authorities have been created under the Income-tax Act, 1961, but still retaining the normal provisions for assessments of appeals in the Income-tax Act about the remedial forums or the appeal mechanisms and the Income-tax Appellate Tribunal constituted under section 253 of the Act continues to be the final fact finding body under the Act even with regard to the assessments of the international transactions under the Special Chapter X as aforesaid and the appeal

to the constitutional courts as provided in section 260A to the High Court and section 261 to the hon'ble Supreme Court are applicable to these special assessments under Chapter X as well."

Now we would like to refer to the findings, reasons, analysis and scrutiny undertaken/given by the Tribunal in its order for excluding the comparables suggested by the Transfer Pricing Officer on the touchstone of comparability to match with the functions performed by the assessee. **11**

11.1 Paragraph Nos. 4 and 5 of the Tribunal's order pertaining to exclusion of IDFC Investment Advisors Pvt. Ltd. reads thus :

"4. We have considered the submissions of the parties and perused the material available on record in the light of the decisions relied upon. On a perusal of the annual report of this company, it is very much clear that the company is engaged in providing PMS and such service is fee based. That apart, reference to the profit and loss account does indicate that the company, though, has earned revenue from different segments such as portfolio management fee, performance fee, advisory fee, etc., but the segmental details are not available. Further, we have also noted from the annual report of the company that it has made investment and also incurred brokerage expenses. If we compare the assessee's activities with the comparables, it could be seen that the assessee is only providing advisory service to its associated enterprises which is non-binding in nature, therefore, is totally different from the functions performed by IDFC. Considering the aforesaid aspect, the Tribunal, Mumbai Bench, in *Carlyle India Advisors Pvt. Ltd.* (supra), has held that this company is not comparable to an investment advisor service provider. Same view has also been expressed by the Tribunal, Mumbai Bench, in *AGM India Advisors Pvt. Ltd.* v. *Deputy CIT* I. T. A. No. 4757/Mum./2015, the assessment year 2010–11, order dated May 18, 2016, and *7 FIL Capital Advisors India Pvt. Ltd.* other decisions of the Tribunal, Mumbai Bench, relied upon by the learned senior counsel. The Bench in the case of *AGM Advisors India Pvt. Ltd.* (supra), ultimately concluded as under :

'7. We find that the assessee objected to the inclusion of ICRA–O and IDFC on the ground that the Transfer Pricing Officer had applied no scientific method in arriving at the said two companies that the companies had been cherry – picked by the Transfer Pricing Officer and he had not furnished the process applied by which he had come to select the said two companies, that such an approach to select comparables was impermissible in law and on that count alone the

said two companies should be rejected, that the first appellate authority had rejected ICRA–O as comparable on investment advisory services rendered by the assessee and had stated the assessee's knowledge process outsourcing division provided financial and analytical services and support of clients in the areas of data extraction, aggregation, electronic conversion of financial statements, validation and analysis, accounting and finance, research and analytics, that the company was not engaged in investment advisory or consultancy services, that the Assessing Officer was directed to exclude ICRA–O from the final set of comparable companies, that he had held that it was functionally not comparable to the assessee. Charging of fees by ICRA–O did not mean that it was a valid comparable to the assessee. As per the settled principles of transfer pricing for a company to be treated as a valid comparable the functions performed, assets employed and risks assumed have to be comparable and not nomenclatures in the annual accounts. We would like to refer to page 507 of the paper book in case of ICRA–O and it reads as under :

"ICRA Online Limited is a leading information services, outsourcing and technology solutions provider and caters for some of the biggest names in the financial services sector in (India) and abroad, which is a testimony to its product quality, commitment and credibility."

From the above description it is clear that ICRA–O operated in two strategic lines of business, i.e., knowledge process outsourcing and information services and technology solutions, with a list of reputed global and domestic clients. Note c (iii) on page 507 of the paper book also proves that the activities performed by the company under the business line "Outsourced Services" were in the nature of "maintenance and management of data" and therefore cannot be compared with the assessee. As far as IDFC is concerned, we would like to mention that a portfolio manager is a body corporate who pursuant to a contract or arrangement with the client would advice or direct or undertake on behalf of the client—whether as a discretionary portfolio manager or otherwise. FAR analysis of a portfolio manager cannot be compared with an assessee engaged in the business of providing investment advisory services. The Tribunal has in the cases discussed at paragraph 6.d.a. held that IDFC was not a valid comparable. Considering the above discussion, we are of the option that the order of the first appellate authority and exclude both the comparables does not suffer from any legal or factual infirmity. So,

confirming his order, we decide the issue against the Assessing Officer.'

5. It is also relevant to observe, the hon'ble jurisdictional High Court in *General Atlantic Pvt. Ltd.* (supra), while approving the view expressed in *Carlyle India Advisors Pvt. Ltd.* (supra) has observed that where a company is remunerated on cost plus basis, it is risk insulated, therefore, on application of FAR, it cannot be compared with other companies if there is any difference. Therefore, respectfully following the decision of the Co-ordinate Bench of the Tribunal referred to above as well as the principle laid down by the hon'ble Jurisdictional High Court, we reject this company as a comparable."

11.2 Paragraph No. 8 of the Tribunal's order pertaining to exclusion of ICRA Online Limited reads thus :

"8. We have considered the submissions of the parties and perused the material available on record in the light of the decisions relied upon. On a perusal of the information submitted in the annual report of this company as well as its financials, we have noted that the functions undertaken by the company are totally different from the assessee. Therefore, the company fails in the FAR analysis itself. For this reason, in the cases relied upon by the learned senior counsel, the Tribunal has held the aforesaid company not comparable to an investment advisory service provider. In this context, we refer to the observations of the Tribunal in *AGM India Advisors Pvt. Ltd.* (supra) reproduced in para 4 hereinabove. Accordingly, we hold that this company is not comparable to the assessee."

11.3 Paragraph Nos. 12 and 13 of the Tribunal's order pertaining to exclusion of Motilal Oswal Investment Advisors Pvt. Ltd. (MOIAPL) reads thus :

"12. We have considered the submissions of the parties and perused the material available on record in the light of the decisions relied upon. Having gone through the annual report of MOIAPL, we have noted that the company is engaged in a number of activities including investment banking activities. Thus, the company is functionally different from the assessee because of functions performed, assets employed and risk undertaken. Therefore, it fails in the FAR analysis itself. It is pertinent to observe, in the case of *Temasek Holding Advisors India Pvt. Ltd.* (supra), Mumbai Bench of the Tribunal, after considering almost similar argument put forward by the parties excluded this company as a comparable to a non–binding investment advisory service provider holding as under :

'25. This comparable has been included by the Transfer Pricing Officer and while including the said comparable he has observed that its income is only from advisory fees during the year and it is performing advisory services in that field of investment like the assessee. Before us, the learned Commissioner of Income-tax-Departmental representative arguing for its inclusion submitted that, if the ICRA Management Services can be included for having revenue from advisory services then on the same analogy this company should also be given the same treatment. From the perusal of the directors' report, it is seen that this company derives its business income from four different business verticals, i.e., equity capital markets, merger and acquisitions, profit equity syndications and structured debt. It also gives advices on cross boarder acquisition. Its core competence is in the field of merchant banking. It also provides comprehensive investment banking solutions and transaction expertise covering private placement of equity, debt and convertible instruments in international and domestic capital markets, monitoring mergers and acquisitions and advising M and A as professional and restructuring advisory and implementations. It is also involved in various professional activities of the merchant banking. A merchant banker provides capital to companies in the form of share ownership instead of loans. It also provides advisory on corporate matters to the companies in which they invest. The focus is on negotiated private equity investment. The wide range of activities include portfolio management, credit syndication, counselling on Mand A, etc. This whole range of functions and activities carried out by Motilal Oswal is definitely are far wider and much different from investment advisory services where core functions is to give advices for making the investments in diversified fields. A company which is engaged in merger and acquisitions, private equity syndication, loan/credit syndication and performing most of the function of a merchant banker, then the entire functions and transactions affects the generation of revenue and margins. Such functions are entirely different from investment advisory services. Mere classification of revenue as "advisory fees" will not put the company in a comparable basket sans functional similarity and transactional analysis. In the case of *Carlyle India Advisors Pvt. Ltd.* (supra), it has been held that, the merchant banking functions are entirely different from investment advisory services and this decision of the Tribunal has been upheld by the hon'ble jurisdictional High Court. Thus, in view of plethora of functional differences as discussed above, we

hold that Motilal Oswal cannot be put into the comparability list and is directed to be excluded.'

13. Following the aforesaid decision, the Tribunal, Mumbai Bench, expressed similar view in the case of *AGM India Advisors Pvt. Ltd.* (supra). In fact, in a host of other decisions cited by the learned senior counsel, the Tribunal has held MOIAPL not to be a comparable to a company involved in investment advisory service as it is an investment banker. The hon'ble jurisdictional High Court also in the decisions relied upon by the learned senior counsel, held that a company engaged in investment banking activity cannot be compared to a company providing investment advisory services. Respectfully following the view taken by the hon'ble jurisdictional High Court as well as different Benches of the Tribunal, we exclude this company from the list of comparables."

11.4 Paragraph Nos. 16 and 17 of the Tribunal's order pertaining to exclusion of Kshitij Investment Advisory Company Limited reads thus :

"16. We have considered the submissions of the parties and perused the material available on record in the light of the decisions relied upon. The fact that there is restructuring of the business of the comparable as a result of realignment with another company is evident from the annual report of the company. Considering the aforesaid aspect, the Tribunal, Mumbai Bench, in *Carlyle India Advisors Pvt. Ltd.* I. T. A. No. 1040/Mum./2015, order dated November 18, 2015 (supra) for the very same assessment year held that this company cannot be treated as a comparable on account of peculiar economic circumstances arising out of its realignment. Relevant observation of the Tribunal is extracted hereunder for the sake of convenience :

'22. We have carefully considered the rival stands on the issue of exclusion of Kshitij Investment Advisory Co. Ltd. from the final set of comparables. The first and the foremost resistance articulated by the Revenue to oppose the exclusion of the said concern from the final set of comparables is the fact that such concern was included by the assessee itself as a comparable in its transfer pricing study. As per the Revenue, since the said concern has been adopted by the assessee as a comparable, it is impermissible for the assessee to raise a plea asking for its exclusion in the process of determination of average margins under the transactional net margin method. In our considered opinion, the proposition being canvassed by the Revenue is not absolute, but it has to be considered in the facts and circumstances of each

case. No doubt in a situation of the type before us, the burden lies on the assessee to justify exclusion of Kshitij Investment Advisory Co. Ltd., considering the fact that initially the assessee had taken it as a good comparable. Our aforesaid approach is founded on a well accepted proposition that in the course of determination of correct tax liability, it is impermissible for the Revenue to take advantage of an ignorance or mistake of the assessee in offering certain amount as income, which is more than the legally due amount. Notably, there cannot be a estoppel against the statute and it is a trite law that no tax can be levied or collected from a subject except by an authority of law. We may hasten to add here that we are not staying that on each and every aspect of the assessment declared in the return of income, an assessee is entitled to turn around and argue differently before the income-tax authorities ; rather, there has to be justifiable reasons shown by the assessee, duly supported by law or facts, whereby the change in stand is merited. In the present case, what the assessee is claiming is that there has been a restructuring/realingment of investment advisory business being carried out by Kshitij Investment Advisory Co. Ltd. which has impacted the financial results thereby rendering the said concern as an unfit comparable. The proposition being canvassed by the assessee is supported by the decision of the Hyderabad Bench of the Tribunal in the case of *Capital IQ Information System (India) Pvt. Ltd.* (supra). In fact, it is quite well understood that in a year where realignment/restructuring of business takes place, such year is often a peculiar economic year in the history of a concern and in such a situation, it would be in the interest of justice and fair play that such a concern is not treated as a comparable. In fact, in principle, we do not find any disagreement on the part of the Transfer Pricing Officer also on this aspect. However, what the Transfer Pricing Officer has stated is that in the present case, the realignment/restructuring is in the same line of business and, therefore, such restructuring/realignment does not result in any change in the activity of business. Therefore, according to the Revenue, there would be no impact on the financial results so as to make it incomparable with the tested transactions. We have carefully considered the aforesaid plea set up by the Revenue and in this context, we may briefly refer to the "Business Review" outlined in the director's report of the said concern, placed at page 536 of the paper book. It is stated therein that the investment advisory business has been realigned and all the employees have been transferred to Everstone Investment Advisors Pvt. Ltd.

during the year under consideration to Everstone Investment Advisors Pvt. Ltd. during the year under consideration with effect from January 1, 2010. The note also suggests that the said concern did not enter into any non-compete agreement with Everstone Investment Advisors Pvt. Ltd. but was free to pursue any activity, including the activity in relation to investment advisory services. The aforesaid aspect has been highlighted by the Revenue to say that the said concern continues to be in the business of rendering investment advisory services and, therefore, the restructuring does not impact the comparability of the concern. In our considered opinion, the approach of the Revenue in this context is quite flawed. Firstly, it is not disputed that the activity of investment advisory services has been realigned which included the transfer of all employees to Everstone Investment Advisory Pvt. Ltd. The averments in the director's report suggest that post realignment, the concern is only evaluating its options to commence business operations either in some other line or in the similar line of investment advisory services. What we are trying to emphasise is that there is no averment in the director's report to suggest that the said concern has actually carried out any investment advisory services post–realignment with effect from January 1, 2010. In fact, in the course of hearing before us, the learned representative for the assessee pointed out that a perusal of the annual report for subsequent financial year of 2010–11 showed no such operations by the said concern. Therefore, considering the aforesaid fact situation, the instant financial year of the said concern is containing peculiar economic circumstances and the same has to be taken into consideration while evaluating the rationale for its inclusion as a comparable. Before us, the learned representative also pointed out that the said restructuring/realignment which has taken place with effect from January 1, 2010, did impact the financial results inasmuch as the income from operations of the said concern for the year under consideration reduced to Rs. 17,23,10,815 from Rs. 26,47,96,102 in the immediately preceding year. Considering the entire conspectus of facts and circumstances, in our view, the assessee-company is justified in asserting that Kshitij Investment Advisory Co. Ltd. deserves to be excluded from the final set of comparables on account peculiar economic circumstances during the year under consideration. Thus, on this aspect also, assessee succeeds.'

17. Following the aforesaid decision, the Tribunal again in the case of *AGM India Advisors Pvt. Ltd.* (supra) held that this company

cannot be treated. As a comparable as these decisions pertain to the very same assessment year and the facts on the basis of which the decisions were rendered by the Tribunal remains same in the case of the present assessee further, as no contrary decision was brought to our notice by the learned Departmental representative, respectfully following the aforesaid decisions of the Co-ordinate Bench, we exclude this company from the list of comparables."

11.5 Paragraph Nos. 24 and 25 of the Tribunal's order pertaining to exclusion of ICRA Management Consulting Service Pvt. Limited reads thus :

"24. We have considered the submissions of the parties and perused the material available on record in the light of the decisions relied upon. From the documentary evidence brought on record by the assessee, we have observed that the assessee is also providing non-binding investment advisory service in various sectors such as infrastructure, retail, telecommunication and networking equipment, health care, financial intermediaries, design and engineering related to infrastructure, media and communication. Thus, as could be seen, though, the service provided by the assessee covers the wide spectrum of activities, however, the nature of service is virtually one, viz., advisory services. The same is the case with the comparable. Though, it is alleged by the learned Departmental representative, the comparable is providing service through various sectors, however, the nature of service is advisory. We have also noted that absolutely similar argument was advanced by the learned Departmental representative in relation to this comparable in the case of *Temasek Holdings Advisors India Pvt. Ltd.* (supra) in the assessment year 2010–11. The Tribunal, after considering the submissions of the learned Departmental representative and also the proposition advanced by him in relation to the principles of res judicata and the decision of Kalpetta Estates Ltd. (supra) relied upon by him in this regard, ultimately treated this company as a good comparable observing as under :

'20. At the outset, this comparable was subject matter of consideration before the Tribunal in the assessment years 2008-09 and 2009-10, wherein this company was held to be good comparable both on the ground of functional similarity and in view of principles of consistency as it was held to be a good comparable by the Transfer Pricing Officer in the earlier years. From the perusal of the annual report, which is appearing from pages 156 to 187 of the paper book, we find that it is essentially providing consultancy services in

diversified areas, like in Government sectors, infrastructure, energy, corporate advisory, banking and financial services, etc. It focuses on consultancy and advisory which is its core area and competency. The revenue generation is purely from consultancy fees which is evident from profit and loss account as on March 31, 2010 (appearing at page 176 of the paper book). The Transfer Pricing Officer in his order has noted that its consultation or advisory operations ranges in various fields which have been tabulated by him at pages 9 to 11 of the order, which according to him the assessee is not performing. On the perusal of the directors' report and also the remarks of the Transfer Pricing Officer, we find that the ICRA Management is providing consultancy services in a myriad areas ranging from development, transportation, urban infrastructure, energy sector, banking and financial services and advising cross border M and A transaction etc. Some other observation made by the Transfer Pricing Officer is that ICRA has participated in various international forums, partnered with foreign company in multiple projects and has a very big client base unlike the assessee. However all these facts do not affect the core competency and functions of the said company, which is advisory, because in all the fields it is rendering only advisory and consultancy services. The whole revenue is again from consultancy/advisory fees. In the instant case also, the assessee is providing investment advisory services to its associated enterprise in diverse industries like, infrastructure, telecom, media, banking, etc., to enable the associated enterprise to take a decision for making investments. The functions of consultancy/advisory have to be seen as its core competence area and not in the field in which such consultancy is given. Under the transactional net margin method , one has to see the transaction undertaken are comparable or not and whether any adjustment is required to obtain a reliable result, because under transactional net margin method the net margin are less affected by transactional differences and is more tolerant to some minor functional differences between controlled and uncontrolled transactions. However, if any unique function or property significantly affects the operating costs or net margin or has a bearing in the generation of revenue itself, then it cannot be considered to be a fit comparable for benchmarking the net margins. Here it is not the case where there is any unique functions materially affecting the revenue or net margins vis-a-vis the functions performed by ICRA. Hence on functional level it is a good comparable. As stated earlier, in the earlier years, the Transfer Pricing

Officer has accepted ICRA to be a comparable and in later years the Tribunal in the assessment years 2008-09 and 2009-10 has held ICRA management to be good comparable qua the functions of the assessee and there being no material change on facts, functional profile or any other factor in this year, then as a matter of consistency, we do not want to deviate from our findings given in the earlier years. There cannot be a pick and choose of comparables every year unless there are some material difference in facts and circumstances compelling to take a different conclusion. Thus, we hold that ICRA management is a good comparable and should be included in the list of final comparables.'

25. Again, in the case *AGM India Advisor Pvt. Ltd.* (supra), the Tribunal, after considering almost similar argument of the learned Departmental representative, followed the decision in *Temasek Holdings Advisors India Pvt. Ltd.* (supra) upholding the company as a comparable. While doing so, the Bench also took note of the decision relied upon by the learned Departmental representative which were also cited before us. Undisputedly, the aforesaid decisions of the Co-ordinate Bench are for the very same assessment year 2010-11. Therefore, respectfully following the aforesaid decisions of the Co-ordinate Bench, we include this company as a comparable."

11.6 Paragraph Nos. 30 and 31 of the Tribunal's order pertaining to exclusion of IDC India Limited reads thus :

"30. We have considered the submissions of the parties and perused the material available on record in the light of the decisions relied upon. On a perusal of the information available in the website and annual report of the company, we have noted that it is primarily engaged in the business of market research and management consultancy. Therefore, the contention of the learned Departmental representative that it is a product company may not be correct. Further, we have noted that in the case of *Temasek Holdings Advisors India Pvt. Ltd.* (supra), the very same argument of IDC India Ltd. being a product company and provides go to market service was advanced by the learned Departmental representative. However, rejecting such contentions of the learned Departmental representative, the Tribunal included this company as a comparable holding as under :

'22. This comparable though accepted by the Transfer Pricing Officer as a good comparable, however, the Dispute Resolution Panel has additionally rejected this comparable. In the assessment year 2008-09, the Tribunal has held to be a good comparable, firstly, on

the ground that this company is also engaged in the advisory and consultancy services for the purpose of investment made in various sectors and secondly, it has been found to be good comparable by the Transfer Pricing Officer in the assessment years 2007-08 and 2009-10. Once the company has been held to be good comparable consistently for three years then without any change in the material facts, it cannot be held that this comparable could be rejected in this year. Moreover, in the case of *Carlyle Advisory India Ltd.*, the Income-tax Appellate Tribunal Mumbai Bench, reported in [2014] 43 taxmann.com 184 (Mumbai-Trib), the Tribunal held that this company is a good comparable with the companies rendering investment advisory services. This decision of the Carlyle Advisors have also been upheld by the hon'ble Bombay High Court. Moreover, we have already discussed the functions performed by the IDC India Ltd. while dealing with learned counsel's argument that functions of advisory services are quite similar to the functions of the assessee and, therefore, we accept the assessee's contention that this comparable cannot be rejected. Accordingly, the same is directed to be included in the comparability list.'

31. In the case of *AGM India Advisors Pvt. Ltd.* (supra), the Co-ordinate Bench after considering the very same argument advanced by the learned Departmental representative and following the decision rendered in *Temasek Holdings Advisors India Pvt. Ltd.* (supra), held that the company is a good comparable. While doing so, the Tribunal had given a categorical finding that IDC India Ltd. is not a product company. Since the aforesaid decisions of the Tribunal are for the very same assessment year, they will squarely apply to the facts of the present case. Moreover, we have noted the fact that in the assessee's own case for the assessment year 2009-10, this company has been accepted as a comparable by the Transfer Pricing Officer/Dispute Resolution Panel. That being the case, we do not see any justifiable reason for excluding this company. As far as the decision rendered in case of *Tevapharm Pvt. Ltd.* (supra), after carefully reading the said order, we have noted that nowhere the Tribunal has held that IDC India Ltd. is a product company. On the contrary, it was excluded since the Tribunal found it functionally dissimilar to that of the assessee. The decision of *Actis Advisors Pvt. Ltd.* (supra) is also factually distinguishable, hence, would not apply. Therefore, respectfully following the decisions of the Co-ordinate Bench of the Tribunal

referred to above, we hold that IDC India Ltd. is a comparable to the assessee."

11.7 Paragraph Nos. 35 and 36 of the Tribunal's order pertaining to exclusion of Informed Technologies Limited reads thus :

"35. We have considered the submissions of the parties and perused the material available on record in the light of the decisions relied upon. On a perusal of the material on record, we have noted that this company is basically engaged in providing data management service to the financial sector. Considering the aforesaid fact, the Tribunal in *Temasek Holdings Advisors (I) Pvt. Ltd.* (supra), while including the company as a comparable has observed as under :

'(v) *Informed Technologies Ltd.* This company mostly offers range of data management services to the financial sector in USA. It collects and analyses data of financial fundamentals, corporate governance and capital market. It outsource services, i.e., BPO services consisting of financial data base and back office activities for research and advisory reports. Thus, the data outsourcing charges are mostly related to analysing of data based on which advise is given for the investment purpose in India. Moreover, this company has been accepted by the Transfer Pricing Officer in the year 2009-10. Thus, it is a good comparable.'

36. We do not find any material difference between the facts in the assessee's case and in the case of *Temasek Holdings Advisors (I) Pvt. Ltd.* (supra) on the basis of which the Tribunal included it as a comparable. Moreover, there is no dispute that the Transfer Pricing Officer has accepted this company as a comparable in the assessee's own case for the assessment year 2009-10. That being the case, in our considered opinion, the company should be treated as comparable to the assessee."

11.8 Paragraph Nos. 41 and 42 of the Tribunal's order pertaining to exclusion of Kinetic Trust Limited reads thus :

"41. We have considered the submissions of the parties and perused the material available on record in the light of the decisions relied upon. The major thrust of argument of the learned Departmental Representative for excluding this company is on account of its low turnover. However, as it appears from the material on record, though, in the show-cause notice the Transfer Pricing Officer proposed to apply a low turnover filter of less than Rs. 1 crore, following the same logic, he should have applied a high turnover filter. Further, in the order passed under section 92CA(3), the Transfer Pricing

Officer has not emphasised the filter finally applied by him and the selection process undertaken, therefore, it cannot be said with any degree of certainty that he applied low turnover filter. Even, assuming that such filter was applied, following the same logic, he should have applied high turnover filter to exclude companies. We have further noted that the Tribunal, Delhi Bench, in *Mckinsey Knowledge Centre India Pvt. Ltd.* (supra) has held that if a company is functionally similar, only because of its low turnover, it cannot be rejected if such turnover filter was not applied either by the assessee or by the Transfer Pricing Officer. The aforesaid observations of the Tribunal, Delhi Bench, was affirmed by the hon'ble Delhi High Court in its judgment referred to above. It is also noteworthy that in the case of *Temasek Holdings Advisors India Pvt. Ltd.* v. *Deputy CIT* I. T. A. No. 776/Mum./2015, the assessment year 2010-11, order dated February 25, 2016, the Co-ordinate Bench after considering virtually identical argument advanced by the Department accepted this company as a comparable. The relevant observations of the Bench is reproduced hereunder for the sake of convenience :

'(ii) Kinetic Trust Ltd. (Rejected by the Transfer Pricing Officer) : Mr. Porus Kaka, submitted that the Transfer Pricing Officer has observed that in the annual report of the Kinetic Trust, does not specify that the said company is engaged in the investment advisory ; further the said company is an NBFC registered with RBI ; and lastly, its turnover is only Rs. 20 lakhs. To counter this Transfer Pricing Officer's observation, Mr. Kaka pointed out that firstly, the directors' report for financial year 2009-10 specifically mentions that the company has concentrated on its main activity of a corporate consultancy services and financial services. This is evident from the directors' report given at page 193 of the paper book. Merely because the said company is an NBFC, the same does not change the nature of activities undertaken by the company, i.e., consultancy services. Secondly, while selecting the list of comparables in search criteria, the assessee has not considered the turnover criteria as one of the factor in determining or streamlining the selection of the companies. It has not cherry picked the comparables by inserting any kind of lower or higher turnover filter. The reliance placed by the Transfer Pricing Officer on the decision of the Tribunal in the case of *Trilogy E-Business Software India P. Ltd.* v. *Deputy CIT* [2013] 23 ITR (Trib) 464 (Bang) (I. T. A. No. 1054/Bang/2011) is not correct as the Tribunal's decision was based on the facts and in that context it has highlighted

the importance to apply the turnover over filter ranging between Rs. 1 crore to Rs. 200 crores. The said decision does not implicate that the range of Rs. 1 crore to Rs. 200 crores is to be applied essentially in all the cases. Thus, the decision of the said Tribunal cannot be applied to the facts of the present case. On the contrary in the case of *Nortel Networks India P. Ltd.*, reported in [2014] 44 taxmann.com 46, the Delhi Tribunal has held that, if the functional profile of the comparable is the same with that of the assessee then, it cannot be excluded from the list of the comparables merely for the reason of low turnover. He submitted that the said decision of the Tribunal has now been upheld by the hon'ble High Court vide order dated February 24, 2015 in I. T. A. No. 3043/2015, wherein, the hon'ble High Court observed that, whether the turnover filter is appropriate one and applicable, cannot be answered in the abstract and is entirely fact dependent. Lastly, the Tribunal in the assessee's own case for the assessment years 2008-09 and 2009-10 has accepted the Kinetic Trust Ltd. as a comparable company so far as the functions performed by the assessee. The learned Transfer Pricing Officer in utter disregard to the Tribunal's order has stated that the said decision of the Income-tax Appellate Tribunal cannot be accepted, because the finding was given on the ground that the Transfer Pricing Officer has accepted this comparable in the earlier years. This cannot be the ground for rejection, rather the Kinetic Trust Ltd. is to be included as the comparable company following judicial precedence and consistency in view of the Tribunal orders for two consecutive earlier years.'

42. The facts on the basis of which the Co-ordinate Bench in *Temasek Holdings Advisors India Pvt. Ltd.* (supra) accepted this company as comparable are more or less similar to the facts involved in the case of present assessee as undisputedly in the assessment year 2009-10, the Transfer Pricing Officer/Dispute Resolution Panel have accepted this company as a comparable. Thus, applying the rule of consistency as well as following the decisions referred to above, we direct the Assessing Officer/Transfer Pricing Officer to include this company as a comparable. In view of the aforesaid, we direct the Assessing Officer/Transfer Pricing Officer to determine the arm's length price afresh in terms of the observations made by us hereinabove."

**12** In view of the above detailed reproduction of the reasonings given by the Tribunal we find that, while undertaking the exercise to arrive at the arm's length price which is essentially a matter of estimate of the fair value

which the Indian company had paid or had received from its associated enterprise , such exercise is required to be undertaken by the Transfer Pricing Officer on the basis of the facts and figures relating to comparable cases of other similarly placed entities, whose relevant data is available in the public domain. As per the provisions of the Act and the Rules, the assessee-company is required to furnish its own transfer pricing analysis and the list of chosen comparables which may or may not be agreed to by the Revenue authorities and they would introduce some more comparables rejecting the comparables given by the assessee-company by applying certain filters like related party transactions (RPT) filter, turnover filter, export earnings filter, employee cost filter, etc. to bring them within the comparable range of the cases of such comparables and generally there would be a tug of war between the assessee and the Revenue in such a situation. We would state that the assessee-company would normally choose comparables, whose operating profit margins are less or only little more than the assessee, but the revenue would bring in comparables with higher profit margins. The Transfer Pricing Officer, may in the case of an assessee introduce and suggest comparables whose operating margins are higher than the assessee-company so as to make transfer pricing adjustments in the declared income of the assessee, resulting in fetching of more revenue. From the aforesaid quoted paragraphs from the Tribunal's order, it is evident that, individual cases of such comparables have been juxtaposed with the functionality of the assessee considered, analysed and discussed by the Tribunal in respect of comparables which were excluded by the Transfer Pricing Officer as also in the case of those comparables which were included by the Transfer Pricing Officer. It is quite common to note that, while some comparables are found to be appropriate and really comparable to the facts of the assessee-company, some are not and it would ultimately result in whether the correct filters have been properly applied or not or whether the most appropriate method of determination of arm's length price has been adopted or not to make fair and reasonable transfer pricing adjustments in the hands of the assessee. However, the entire exercise of making transfer pricing adjustments on the basis of comparables is nothing but a matter of estimate of a broad and fair guess-work of the authorities based on factual relevant materials brought before the authorities, i.e., the Transfer Pricing Officer, the Dispute Resolution Panel and the Tribunal, which are the fact finding authorities.

We would also like to quote paragraph Nos. 16 to 22 from the judgment **13**
in the case of *Pr. CIT* v. *Softbrands India Pvt. Ltd.* (supra), which refers to comparative analyses of section 260A of the said Act and sections 100 and

103 of the Code of Civil Procedure, 1908 in order to justify what would be a substantial question of law in such a case (page 524 of 406 ITR) :

"We would analyse the provisions of section 260A of the Act in a little more detail but we are of the firm opinion that the entry into the High Court under section 260A of the Act is locked with the words 'Substantial questions of law' and the key to open that lock to maintain such appeal can only be the perversity of the findings of the Tribunal in these type of cases and the perversity in the findings is not only averred by the appellant before this court but, established on the basis of cogent material which was available before the authorities below including the Tribunal and the findings arrived at by the Tribunal can be so held to be perverse within the well settled parameters for determining the same as perverse. It is not allowed to either of the parties, i.e., the assessee or the Revenue to invoke the jurisdiction of this court under section 260A of the Act merely because the Tribunal comes to reverse or modify the findings given by the lower authority, viz., Transfer Pricing Officer or Dispute Resolution Panel (DRP) which comprises of three Commissioners and the Revenue or the assessee may feel dissatisfied, because of the reversal or modification of such findings by the Tribunal resulting in leaving out of certain comparables or adding on of certain comparables for determining the 'arm's length price' in the hands of the assessee-company.

Unless such perversity in the findings of the Tribunal is established we are of the opinion that the appeals under section 260A of the Act cannot and should not be entertained at the instance of either of the parties and the present cases before us, we find that the Tribunal has given cogent reasons and detailed findings upon discussing each case of comparable corporate properly and therefore, we find ourselves unable to call such findings of the Tribunal perverse in any manner so as to require our interference under section 260A of the Act.

We now take up the analysis of section 260A of the Act which we have already said is in pari materia with sections 100 and 103 of the Civil Procedure Code.

The said provisions are quoted below for ready reference and comparison.

Section 260A of the Income-tax Act, 1961 reads as under :

'260A. *Appeal to High Court*.—(1) An appeal shall lie to the High Court from every order passed in appeal by the Appellate Tribunal before the date of establishment of the National Tax Tribunal, if the

High Court is satisfied that the case involves a substantial question of law.

(2) The Principal Chief Commissioner or Chief Commissioner or the Principal Commissioner or Commissioner or an assessee aggrieved by any order passed by the Appellate Tribunal may file an appeal to the High Court and such appeal under this sub-section shall be—

(a) filed within one hundred and twenty days from the date on which the order appealed against is received by the assessee or the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner ; . . .

(c) in the form of a memorandum of appeal precisely stating therein the substantial question of law involved.

(2A) The High Court may admit an appeal after the expiry of the period of one hundred and twenty days referred to in clause (a) of sub-section (2), if it is satisfied that there was sufficient cause for not filing the same within that period.

(3) Where the High Court is satisfied that a substantial question of law is involved in any case, it shall formulate that question.

(4) The appeal shall be heard only on the question so formulated, and the respondents shall, at the hearing of the appeal, be allowed to argue that the case does not involve such question :

Provided that nothing in this sub-section shall be deemed to take away or abridge the power of the court to hear, for reasons to be recorded, the appeal on any other substantial question of law not formulated by it, if it is satisfied that the case involves such question.

(5) The High Court shall decide the question of law so formulated and deliver such judgment thereon containing the grounds on which such decision is founded and may award such cost as it deems fit.

(6) The High Court may determine any issue which—

(a) has not been determined by the Appellate Tribunal ; or

(b) has been wrongly determined by the Appellate Tribunal, by reason of a decision on such question of law as is referred to in sub-section (1).

(7) Save as otherwise provided in this Act, the provisions of the Code of Civil Procedure, 1908 (5 of 1908), relating to appeals to the High Court shall, as far as may be, apply in the case of appeals under this section.'

Sections 100 and 103 of the Code of Civil Procedure, 1908 read thus :

'100. *Second Appeal.*—(1) Save as otherwise expressly provided in the body of this Code or by any other law for the time being in force, an appeal shall lie to the High Court from every decree passed in appeal by any court subordinate to the High Court, if the High Court is satisfied that the case involves a substantial question of law.

(2) An appeal may lie under this section from an appellate decree passed ex parte.

(3) In an appeal under this section, the memorandum of appeal shall precisely state the substantial question of law involved in the appeal.

(4) Where the High Court is satisfied that a substantial question of law is involved in any case, it shall formulate the question.

(5) The appeal shall be heard on the question so formulated and the respondent shall, at the hearing of the appeal, be allowed to argue that the case does not involve such question :

Provided that nothing in this sub-section shall be deemed to take away or abridge the power of the court to hear, for reasons to be recorded, the appeal on any other substantial question of law, not formulated by it, if it is satisfied that the case involves such question.'

'103. *Power of High Court to determine issue of fact.*—In any second appeal, the High Court may, if the evidence on the record is sufficient, determine any issue necessary for the disposal of the appeal,—

(a) which has not been determined by the lower appellate Court or both by the court of first instance and the lower Appellate Court, or

(b) which has been wrongly determined by such court or courts by reason of a decision on such question of law as is referred to in section 100.'

What is a substantial question of law ?

20. From a bare comparison of the provisions quoted above and as discussed in various judgments of the Constitutional Courts, which we will refer in brief hereinbelow, it is clear that the Scheme of both section 260A in the Income-tax Act, 1961 and section 100 read with section 103 of the Code of Civil Procedure are in pari materia and in same terms.

21. The existence of a substantial question of law is sine qua non for maintaining an appeal before the High Court. While the appeal to High Court under section 260A of the Act may be a first appeal in the sense from the order of final fact finding by the Tribunal under the Income-tax Act, whereas the second appeal on substantial question of law before High Court under section 100 would lie against the judgment and decree of the first appellate court disposing of an appeal against the judgment and decree of a trial court, but none the less it is the third round of consideration at the level of the High Court, where the facts and law both have been screened, discussed and analysed by the authorities or the courts below and therefore the tenor and colour of the words 'substantial question of law' in both these enactments remains the same.

22. The High Court has power to not only formulate the substantial questions of law and rather it has the duty to do so and can also frame additional substantial questions of law at a later stage, if such a substantial question of law is involved in the appeal before it under these provisions and the appeal should be heard and decided only on such substantial questions of law after allowing the parties to address their arguments on the same. The extended power given to the High Courts to decide even an issue under sub-section (6) of section 260A of the Income-tax Act, which is in pari materia with section 103 of the Civil Procedure Code and which says that the High Courts may determine any issue which (a) has not been determined by the Tribunal or (b) has been wrongly determined by the Tribunal, can be so determined by the High Court, only if the High Court comes to the conclusion that 'by reason of the decision on substantial question of law rendered by it', such a determination of issue of fact also would be necessary and incidental to the answer given by it to the substantial question of law arising and formulated by it."

**14** Section 92A defines an associated enterprise in relation to another enterprise to mean an enterprise which participates directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise by holding not less than 26 per cent. of the voting power in the other enterprise and satisfies the other criteria as stated in section 92A of the Act.

14.1. Relevant portion of section 92B of the Act reads thus :

"'international transaction' means a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible

property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises, and shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises."

14.2. Section 92C(1) of the Act reads thus :

"(1) The arm's length price in relation to an international transaction or specified domestic transaction shall be determined by any of the following methods, being the most appropriate method, having regard to the nature of transaction or class of transaction or class of associated persons or functions performed by such persons or such other relevant factors as the Board may prescribe, namely :

(a) comparable uncontrolled price method ;

(b) resale price method ;

(c) cost plus method ;

(d) profit split method ;

(e) transnational net margin method ;

(f) such other method as may be prescribed by the Board."

14.3. Section 92CA deals with reference to Transfer Pricing Officer where an assessee has entered into an international transaction a specified domestic transaction and the Assessing Officer considers it necessary or expedient, he may with the previous approval of the Principal Commissioner or Commissioner refer the computation of the arm's length price in relation to the said international transaction or specified domestic transaction to the Transfer Pricing Officer.

14.4. Section 92F(ii) of the Act defines "arm's length price" and reads thus :

"(ii) 'arm's length price' means a price which is applied or proposed to be applied in a transaction between persons other than associated enterprises, in uncontrolled conditions ;"

**15** In the case before us the transactional net margin method appears to have been the most popular and widely adopted method for determining the arm's length price in which the operating profit margin of comparable companies are considered by the authorities and applied to the case of the assessee to determine the arm's length price to make transfer pricing adjustments. Rules 10A, 10AB, 10B, 10C and 10CA of the Income-tax

Rules, 1962 prescribe the manner for working out arm's length price under the prescribed methods. From the aforesaid scheme of assessment, it is clear that the process of determination of arm's length price has to be undertaken by the Expert Wing of the Income-tax Department which is manned by Transfer Pricing Officer and at the higher level by a collegium of three Commissioners in the form of Dispute Resolution Panel whose orders are appealable before the Appellate Tribunal. In the above backdrop, in so far as the present case is concerned the Transfer Pricing Officer had rejected six comparable companies chosen by the assessee for benchmarking, namely, (i) Access India Advisors Limited ; (ii) ICRA Management Consulting Services Limited ; (iii) IDC (India) Limited ; (iv) Informed Technologies Limited ; (v) Integrated Capital Services Limited and (vi) Kinetic Trust Limited. The Transfer Pricing Officer only accepted one company as a comparable company being Future Capital Investment Advisors Limited but undertook a further detailed analyses and proposed to include the following five more companies as comparables, namely, (i) Future Capital Holdings Limited (Segmental) ; (ii) ICRA Online Limited (Segmental) ; (iii) IDFC Investment Advisors Private Limited ; (iv) Kshitij Investment Advisors Limited and (v) Motilal Oswal Investment Advisors Private Limited.

The submissions advanced on behalf of the respective parties are mostly **16**
based upon the filters which have been applied which are essentially related to turnover filter, the comparable entities being functional entities, higher transfer pricing adjustments, transfer pricing analyses and profits declared by the companies. We have quoted the specific findings given by the Tribunal and would therefore, not like to delve deeper or reiterate the same. We would however like to say that the Tribunal has considered the case of each comparable company and discussed the parameters of comparables for the purposes of including the same as a comparable and/or excluding the same as comparable on the basis of the functionality of the said companies in the public domain. We find that such a detailed exercise having been undertaken by the Tribunal qua each and every comparable company, the reasons given by the Tribunal cannot be faulted with in respect of the comparable companies. The Tribunal has referred to and relied upon the order passed by this court in the case of *Pr. CIT* v. *Temasek Holdings Advisors India Pvt. Ltd.* in Income Tax Appeal No. 304 of 2017 delivered on April 16, 2019, wherein the following substantial questions of law were framed :

> "(a) Whether on the facts and in the circumstances of the case, the Tribunal is correct in law in directing the Assessing Officer to include

ICRA Management Consultancy Services Ltd., Kinetic Trust Limited in the set of comparable companies while determining the TP adjustment of international transaction ?

(b) Whether on the facts and in the circumstances of the case, the Tribunal is correct in law in striking down the additional markup margin of 3 per cent. to the average PLI of the comparable companies selected by the Transfer Pricing Officer ?"

17 In the said order, this court after referring to another order dated November 17, 2016 passed in Income Tax Appeal No. 1051 of 2014 dismissed the Revenue's appeal raising objection to the Tribunal's decision to include ICRA Management Consultancy Services Ltd. and Kinetic Trust Limited which were both rejected by the Transfer Pricing Officer. So also in the present case, the comparables suggested by the assessee which were excluded by the Transfer Pricing Officer/Dispute Resolution Panel were in fact adopted as comparables by the Transfer Pricing Officer for the financial year 2009-10 in the case of the assessee itself. This aspect was also considered in the aforesaid order.

18 The assessee has placed before us a copy of the judgment delivered by this court in the case of *Pr. CIT* v. *Bain Capital and Advisors (I) P. Ltd.* in Income Tax Appeal No. 541 of 2016, dated November 24, 2018, wherein the Revenue had urged the following question for consideration.

"Whether on the facts and in the circumstances of the case and in law, the Tribunal was justified in holding that Motilal Oswal Investment Advisors Pvt. Ltd. and M/s. IDFC Ltd. were not comparables for the purpose of rule 10B of the Income-tax Rules ?"

19 This court after due consideration dismissed the appeal of the Revenue holding that no substantial question of law arose from the order of the Tribunal.

20 On a thorough consideration we find that the rationale for inclusion of the six comparables excluded by the Transfer Pricing Officer have been dealt with in extensive detail by the Tribunal and we are in agreement with the reasons recorded by the Tribunal. Further the reasons given for inclusion of the five new comparables by the Transfer Pricing Officer have been decidedly set aside by the Tribunal on the basis of decisions rendered by this court either in the case of the assessee itself and/or in other cases after proper consideration.

21 At this stage we would like to refer to paragraph No. 54 in the judgment of *Pr. CIT* v. *Softbrands India Pvt. Ltd.* (supra), which reads thus (page 540 of 406 ITR) :

> "The procedure of assessment under Chapter X relating to international transactions as indicated above is already a lengthy one and involves multiple authorities of the Department. A huge, cumbersome and tenacious exercise of transfer pricing analysis has to be undertaken by the corporate entities who have to comply with the various provisions of the Act and Rules with a huge data bank and in the first instance they have to satisfy that the profits or the income from transactions declared by them is at 'arm's length' which analysis is invariably put to test and inquiry by the authorities of the Department and through the process of Transfer Pricing Officer (TPO) and Dispute Resolution Panel (DRP) and the Tribunal at various stages, the assessee has a cumbersome task of compliance and it has to satisfy the Authorities that what has been declared by them is true and fair disclosure and much of the transfer pricing adjustments is not required but the tax authorities have their own view on the other side and the effort on the part of the tax Revenue authorities is always to extract more and more revenue. This process of making huge transfer pricing adjustments results in multi layer litigation at multiple fora. After the lengthy process of the same, the matter reaches the Tribunal which also takes its own time to decide such appeals. In the course of this dispute resolution, much has already been lost in the form of time, man-hours and money, besides giving an adverse picture of the sluggish dispute resolution process through these channels. If appeals under section 260A of the Act were to be lightly entertained by High Court against the findings of the Tribunal, without putting it to a strict scrutiny of the existence of the substantial questions of law, it is likely to open the flood-gates for this litigation to spill over on the dockets of the High Courts and up to the Supreme Court, where such further delay may further cause serious damage to the demand of expeditious judicial dispensation in such cases."

From the above, it is clear that the appeal filed under section 260A of **22**
said Act is required to be entertained only on "substantial question of law" arising out of the order of the Tribunal, keeping in mind that we cannot disturb findings of fact under section 260A of the said Act unless such findings are shown to be ex facie perverse and unsustainable and exhibit a total non-application of mind. We are therefore of considered opinion that the present appeal filed by the Revenue does not give rise to any substantial question of law. The appeal filed by the Revenue is found to be devoid of merit and the same is liable to be dismissed.

**23** In view of the above findings, the appeal filed by the Revenue is therefore dismissed with no order as to costs.

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**[2020] 424 ITR 602 (Delhi)**

[IN THE DELHI HIGH COURT]

## ASSISTANT COMMISSIONER OF INCOME-TAX

*v.*

## V. K. GUPTA

**VIBHU BAKHRU** J.

February 17, 2020.

**SS ▸ ITA 1961 s 276CC**
**AY ▸ 2008-09**
**HF ▸ Assessee**

OFFENCES AND PROSECUTION—WILFUL DELAY IN FILING RETURNS—FINDING THAT DELAY WAS NOT WILFUL—CONVICTION UNDER SECTION 276CC NOT VALID—INCOME-TAX ACT, 1961, S. 276CC.

*Search and seizure operations under section 132 of the Income-tax Act, 1961, were conducted in respect of a group of concerns. This included search in the premises occupied by the assessee and his brother. The assessee and his brother were residing in different floors of the same premises. Thereafter, on April 21, 2010, a notice under section 153A was issued to the assessee calling upon the assessee to furnish a return. The assessee did not file the return on time. He contended that due to family disputes and unavoidable reasons, he did not have the details or copies of the returns and that there was no mala fide intention on his part for failure to comply with the notice under section 153A. Subsequently, on December 14, 2011, the assessee filed the requisite return in the prescribed form. The Revenue filed a complaint under section 276CC on account of failure on the part of the assessee to file a return for the assessment year 2008-09, in compliance with the notice under section 153A. Thereafter, the assessee was convicted. The single judge held that the default committed by the assessee was not wilful. On further appeal :*

Held, *dismissing the appeal, that copies of certain documents were provided to the representatives of the assessee. However, it was not disputed that copies of all material documents seized during the search and seizure operations were not provided to the assessee. Admittedly, the assessee was also not provided the copy of the panchnama in respect of the documents seized from the premises occupied by his brother. More importantly, it was not disputed*

*that the assessee had not sent several letters, seeking copies of the documents for the purpose of filing the returns. But copies of all the documents seized had not been provided to the assessee. It also had to be noted that the returns were filed in due course. Hence, the conviction under section 276CC was not valid.*

**Crl. L. P. No. 263 of 2017 and Crl. M. A. No. 7410 of 2017.**

*Ms. Vibhooti Malhotra*, Senior Standing Counsel, with *Shailender Singh* and *Siddharth Manocha*, for the petitioner.

*Yogesh Jagia*, *Amit Sood*, *Rishabh Nangia* and *Ms. Sumedha Chadha*, Advocates, for the respondent.

**JUDGMENT**

VIBHU BAKHRU J.—The Revenue has filed the present petition impugning an order dated November 28, 2015 passed by the learned Special Judge-IV, (PC Act) CBI, Delhi, whereby the respondent's appeal against an order dated June 26, 2015 passed by the learned Additional Chief Metropolitan Magistrate convicting the respondent of an offence punishable under section 276CC of the Income-tax Act, 1961 (hereafter "the Act"), was allowed and the respondent was acquitted of committing the said offence. 1

The Revenue alleged that the respondent had wilfully defaulted in filing a return pursuant to the notices issued under section 153A of the Act and thus, committed the offence punishable under section 276CC of the Act. 2

The aforesaid controversy arises in the following context : 3

3.1 That search and seizure operations under section 132 of the Act were conducted in respect of Standard Watch Group of Concerns. This included search in the premises occupied by the respondent and his brother – premises bearing No. S-511, Greater Kailash Part-II, New Delhi. The respondent and his brother S. K Gupta were residing in different floors of the same premises. Thereafter, on April 21, 2010, a notice under section 153A of the Act was issued to the respondent calling upon the respondent to furnish a return in respect "of the company in which you are assessable for the assessment year 2008-09" within sixteen days of the service of the said notice. Thereafter, a show-cause notice dated November 15, 2010 was issued to the respondent. Subsequently, another notice dated June 6, 2011 (exhibit PW-1/5) under section 153A of the Act was issued, calling upon the respondent to file a return of income in respect of "the individual/company in which you are assessable for the assessment year 2008-09" in the prescribed form within a period of fifteen days from the service of the said notice. This was followed by a show-cause notice dated August 11, 2011, calling upon the respondent to show-cause as to why action should not be

taken against him for not filing the return as required. The respondent responded to the said notice and relying upon his response to the earlier show-cause notice (letter dated October 12, 2010, which was filed on November 26, 2010). He stated that the complete records relating to income-tax returns including relevant data, photocopies and relevant documents were in the possession of his brother, who was responsible for income-tax compliances and filing of income-tax returns for the whole family. The respondent further stated that there were certain disputes between his family and his brother (Shri Suresh Gupta) and the complete records had not been returned by Shri Suresh Gupta to him or his family. He stated that he had no copies of the earlier returns and/or related documents. However, he further stated that the return filed earlier be treated as a return in response to the notice under section 153A of the Act.

3.2 The respondent contended that due to family disputes and unavoidable reasons, he did not have the details or copies of the returns. And, there was no mala fide intention on his part for the non-compliance of the notices under section 153A of the Act.

3.3 Subsequently on December 14, 2011, the respondent filed the requisite return in the prescribed form.

3.4 The Revenue filed a complaint under section 276CC of the Act on account of failure on the part of the respondent to file a return for the assessment year 2008-09, in compliance with the notice under section 153A of the Act.

3.5 Subsequently, the assessment under section 153A read with section 143(3) of the Act was framed, assessing the total income at Rs. 25,97,13,590 and a notice demanding Rs. 14,06,55,223 was issued. Thereafter, a show-cause notice was issued for the offence punishable under section 276CC of the Act.

3.6 The respondent was summoned and he pleaded no guilty and the complaint was set down for trial.

3.7 The respondent raised several defences, including (a) that the notices issued were vague ; (b) there was no proper sanction for launching the prosecution ; and (c) there was no wilful default on the part of the respondent, as he did not have necessary documents for filing the return.

3.8 The learned Metropolitan Magistrate did not accept the aforesaid contentions and convicted the respondent for committing an offence punishable under section 276CC of the Act by an order dated June 26, 2015. Thereafter, by an order dated June 29, 2015, the respondent was sentenced to undergo simple imprisonment for a period of one year with a fine

of Rs. 20,000 and in default of payment of fine, to undergo simple imprisonment for a further period of fifteen days.

3.9 Aggrieved by the same, the respondent preferred an appeal, which was allowed by an order dated November 28, 2015 (which is impugned herein by the Revenue Department).

3.10 The learned special judge (appellate court) did not accept the contention that the notices were vague or that the sanction for prosecution was not proper. However, the appellate court held that the default committed by the respondent was not wilful. The appellate court, essentially, accepted the respondent's contention that he did not have the necessary documents and although he had applied for the copies of the documents seized by the income-tax authorities, the same were not supplied to him and therefore, his failure to file the return in response to the notice under section 153A of the Act could not be held to be wilful.

Ms. Malhotra, learned counsel appearing for the Revenue contended **4** that the appellate court had grossly erred in accepting that the respondent was not a wilful defaulter. She submitted that in terms of section 278E of the Act, existence of a culpable mental state on the part of the accused is assumed. She submitted that, therefore, the failure to file the return would necessarily have to be assumed as wilful, unless established to the contrary. She submitted that the respondent had not led any evidence to establish that the default was not wilful and he had not pointed out any specific document that was not provided to him and had impeded his filing the return as required.

At the outset, it is relevant to observe that it is an admitted case that the **5** copies of all the documents, which were seized during the search and seizure operations, were not provided to the respondent.

The respondent had sent a letter clearly stating that there were disputes **6** between him/his family. And, his brother and his brother was responsible for income-tax compliances for the whole family and was in possession of the necessary documents. The respondent had claimed that the businesses were being conducted jointly under six companies. During trial, the LDC of the Company Law Board deposed as a witness for defence (DW-2) and his testimony established that there were disputes between the respondent and his brother relating to the affairs of their companies in which businesses were carried out.

Concededly, the respondent had issued a letter dated April 27, 2010 **7** requesting for inspection and copies of the seized material in reference to the notice under section 158A of the Act. It is material to note that the request was not only for the material documents seized from the part of the

premises occupied by the respondent, but also for the material seized during search, which also included the documents seized from the floor of the premises occupied by his brother. The respondent had also sought statement of various persons recorded during search. The said letter dated April 27, 2010 (exhibit DW-1/D), clearly indicates that the respondent specifically indicated that the said documents were required "for the purpose of complying and preparing the returns".

8 Ms. Malhotra earnestly contended that several documents were provided to the respondent and had referred to the noting on the letter dated August 18, 2009 (exhibit PW-2/2), which indicated that copies of VA-1 to VA-17 had been received by the representative of the respondent. She contended that in the circumstances, it was incumbent on the respondent to specify which particular document was required by him and further establish that non-receipt of that document had prevented him from filing the return.

9 The said contention is unpersuasive. The respondent had sent a letter (exhibit PW-2/1) dated September 12, 2009, requesting for copies of the seized material. The noting on the said material indicates that the respondent was asked to pay a sum of Rs. 500 to the Public Relations Officer, Income Tax Department, CR Building, New Delhi. Admittedly, the respondent had paid the said amount and communicated the same by a letter dated August 18, 2009 (exhibit PW-2/2). It appears from the noting that copies of certain documents (VA-1 to VA-17) were provided to the representatives of the respondent. However, it is not disputed that copies of all material/documents seized during the search and seizure operations were not provided to the respondent. Admittedly, the respondent was also not provided the copy of the panchnama in respect of the documents seized from the premises occupied by his brother. More importantly, it is not disputed that the respondent had sent several letters, including letters dated April 27, 2010 (exhibit DW-1/D) and May 20, 2010 (exhibit DW-1/C), seeking copies of the documents for the purpose of filing the returns. But copies of all the documents seized had not been provided to the respondent.

10 The contention that the respondent was further required to specify the document which was required by him for filing the return, to rebut the presumption of culpable mental state, is unpersuasive. The returns for the relevant assessment year had already been filed in due course. The respondent was now called upon to once again file the return pursuant to the alleged incriminating material seized during the search and seizure operations. Plainly, in the circumstances, it would be necessary for the

respondent to examine all material documents seized during the search and seizure operations before filing the return. The respondent had already indicated his difficulty in doing so in view of the family disputes and had requested for inspection of the copies of all documents seized during the raid.

In the given circumstances, the appellate court had concluded that the respondent's failure to file the return at the material time could not be considered as wilful. **11**

This court finds no fault with the trial court's view. Undeniably, it is a plausible one and, therefore, warrants no interference by this court. **12**

The petition is, accordingly, dismissed. The pending application is also disposed of. **13**

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**[2020] 424 ITR 607 (SC)**

[IN THE SUPREME COURT OF INDIA]

## NEW DELHI TELEVISION LTD.

*v.*

## DEPUTY COMMISSIONER OF INCOME-TAX

L. NAGESWARA RAO and DEEPAK GUPTA JJ.

April 3, 2020.

**SS ▸ ITA 1961, ss 147, 148**
**AY ▸ 2008-09**
**HF ▸ Department/Assessee**

REASSESSMENT—INCOME ESCAPING ASSESSMENT—GENERAL PRINCIPLES—DISPUTE RESOLUTION PANEL FOR SUCCEEDING ASSESSMENT YEAR RAISING DOUBTS AS TO CORPORATE STRUCTURE OF ASSESSEE AND ITS SUBSIDIARIES AND TAX EVASION PETITIONS BY SHAREHOLDERS SHOWING EVIDENCE OF ROUND TRIPPING OF ASSESSEE'S UNDISCLOSED INCOME THROUGH SUBSIDIARIES—MATERIAL SUFFICIENT TO FORM REASON TO BELIEVE THAT INCOME HAD ESCAPED ASSESSMENT—INCOME-TAX ACT, 1961, ss. 147, 148.

REASSESSMENT—LIMITATION—EXTENDED PERIOD—ASSESSING OFFICER AWARE OF ENTITIES WHICH HAD SUBSCRIBED TO CONVERTIBLE BONDS—ALL RELEVANT FACTS, i. e., ENTITIES WHO HAD SUBSCRIBED TO BONDS, THEIR ADDRESSES AND CONSIDERATION PAID BY EACH, WITHIN KNOWLEDGE OF ASSESSING OFFICER—FULL AND TRUE DISCLOSURE BY

ASSESSEE OF ALL MATERIAL FACTS NECESSARY FOR ASSESSMENT—INCOME-TAX ACT, 1961, SS. 147, 148.

REASSESSMENT—LIMITATION—EXTENDED PERIOD OF 16 YEARS WHERE FOREIGN ASSET INVOLVED—NOTICE—NO MENTION OF FOREIGN ASSETS—NOTHING IN REASONS TO INDICATE INTENTION TO APPLY EXTENDED PERIOD OF 16 YEARS—NOTICE AND REASONS GIVEN THEREAFTER NOT CONFORMING TO PRINCIPLES OF NATURAL JUSTICE—INCOME-TAX ACT, 1961, S. 147, *second prov.*

*Merely the fact that the original assessment is a detailed one cannot take away the powers of the Assessing Officer to issue notice under section 147 of the Income-tax Act, 1961. An Assessing Officer can only reopen an assessment if he has "reason to believe" that undisclosed income has escaped assessment. Mere change of opinion of the Assessing Officer is not sufficient to meet the standard of "reason to believe".*

*Subsequent facts which come to the knowledge of the Assessing Officer can be taken into account to decide whether or not the assessment proceedings should be reopened. Information which comes to the notice of the Assessing Officer during proceedings for subsequent assessment years can definitely form tangible material to invoke powers vested with the Assessing Officer under section 147 of the Act.*

*It is the duty of the assessee to disclose fully and truly all material facts which are primary facts. Disclosure of other facts which may be termed secondary facts is not necessary.*

*The assessee-company ran television channels. It had a subsidiary based in the United Kingdom. The U. K. subsidiary had issued step-up coupon bonds amounting to US $ 100 million in July, 2007 through the Bank of New York for a period of 5 years. The issue was arranged by J and the funds were received by the U. K. subsidiary through the Bank of New York. The assessee had agreed to furnish a corporate guarantee for this transaction. These bonds were subscribed by various entities and were to be redeemed at a premium of 7.5 per cent. after the expiry of the period of 5 years. However, these bonds were redeemed in advance at a discounted price of US $ 74.2 million in November, 2009. For the assessment year 2008-09 it filed a return declaring a loss. The Assessing Officer held that the U. K. subsidiary had virtually no financial worth, it had no business and could not have issued convertible bonds of US $ 100 million, unless the repayment with interest was secured, that this was secured only because of the assessee agreeing to furnish guarantee in this regard. He held that the transaction should be treated like a guarantee issued by any corporate guarantor in favour of another corporate entity.*

*The Assessing Officer did not doubt the validity of the transaction but imposed a guarantee fee at 4.68 per cent. treating it as a business transaction and added Rs. 18.72 crores to the income of the assessee. On March 31, 2015, the assessment was reopened mainly on the basis of the order of the Dispute Resolution Panel for the following assessment year, 2009-10, to the effect that monies raised by the assessee through its subsidiaries in the Netherlands and the U. K. subsidiary represented sham transactions through which undisclosed income, for which tax had not been paid, was brought back to India by circuitous round-tripping. The Assessing Officer took the view that the U. K. subsidiary had a capital of only Rs. 40 lakhs and no business activities in the United Kingdom except a postal address and that the natural inference was that it was the assessee's own funds introduced in the U. K. subsidiary in the garb of the bonds. Complaints had been received from a minority shareholder alleging that the money introduced in the U. K. subsidiary was shifted to another subsidiary of the assessee in Mauritius from where it was taken to a subsidiary of the assessee in Mumbai and finally to the assessee. The U. K. subsidiary itself was placed under liquidation. Therefore, the Assessing Officer was of the opinion that the amount of Rs. 405.09 crores introduced into the books of the U. K. subsidiary during the financial year 2007-08 corresponding to the assessment year 2008-09 through the transaction involving the step-up coupon convertible bonds pertained to the assessee. The notice also recorded that the escapement was due to failure on the part of the assessee to disclose fully and truly all facts material for assessment. The Assessing Officer did not accept the assessee's objections and held that there was non-disclosure of material facts by the assessee. The assessee filed a writ petition which the High Court dismissed. On appeal :*

Held, *(i) that the assessee's contention that once the transaction of step-up coupon bonds had been accepted to be correct the Department could not reopen it was not sustainable but the genuineness of the transaction would be considered by the concerned Assessing Officer.*

*(ii) That the original order of assessment was passed on August 3, 2012. It was thereafter on December 31, 2013 that the Dispute Resolution Panel in the case of assessment year 2009-10 raised doubts with regard to the corporate structure of the assessee and its subsidiaries. It noted that certain shares of the U. K. subsidiary had been acquired by U of the Netherlands, indirectly by subscribing to shares of the Netherlands subsidiary. The U. K. subsidiary did not have any business activity in London. It had no fixed assets and was not even paying rent. Other than the fact that the U. K. subsidiary was incorporated in the U. K., it had no other commercial business there. The U. K.*

*subsidiary had declared a loss of Rs. 8.34 crores for the relevant year. The assessee was the parent company of the U. K. subsidiary and its dictates were important for running the U. K. subsidiary. The final assessment order for assessment year 2009-10 disclosed similar facts. The tax evasion petitions filed by the minority shareholders of the assessee described in detail the communication between the assessee and the subsidiaries and showed evidence of round tripping of the assessee's undisclosed income through a layer of subsidiaries which led to the issuance of the notice. The material disclosed in the assessment proceedings for the subsequent years and the material placed on record by the minority shareholders formed the basis for taking action under section 147 of the Act. At the stage of issuance of notice, the Assessing Officer had only to form a prima facie view. The material disclosed in the assessment proceedings for subsequent years was sufficient to form such a view. There were reasons to believe that income had escaped assessment in this case.*

*Decision of the Delhi High Court in* NEW DELHI TELEVISION LTD. *v.* DEPUTY CIT [2018] 405 ITR 132 (Delhi) *affirmed on this point.*

CLAGETT BRACHI CO. LTD. *v.* CIT [1989] 177 ITR 409 (SC), ESS ESS KAY ENGINEERING CO. P. LTD. *v.* CIT [2001] 247 ITR 818 (SC) *and* PHOOL CHAND BAJRANG LAL *v.* ITO [1993] 203 ITR 456 (SC) *applied.*

*(iii) That even before the assessment order was passed, the Assessing Officer was aware of the entities which had subscribed to the convertible bonds. The extended period of limitation of 6 years for initiating proceedings under the first proviso to section 147 of the Act could be invoked only if the Department could show that the assessee had failed to disclose fully and truly all material facts necessary for its assessment. The assessee had disclosed all the facts it was bound to disclose. If the Department wanted to investigate the matter further at that stage it could have easily directed the assessee to furnish more facts. The assessee made a disclosure about having agreed to stand guarantee for the transaction by the U. K. subsidiary and it had also disclosed the factum of the issuance of convertible bonds and their redemption. The income, if any, arose because of the redemption at a discounted price. This was an event which took place subsequent to the assessment year in question though it may be income for the assessment year. All relevant facts were duly within the knowledge of the Assessing Officer. The Assessing Officer knew who were the entities who had subscribed to other convertible bonds and in other proceedings relating to the subsidiaries the same Assessing Officer had knowledge of addresses and the consideration paid by each of the bondholders as was apparent from assessment orders passed in the cases of sister companies on the same date. Therefore, there was full and true disclosure of all*

*material facts necessary for its assessment by the assessee. It could not be said that the assessee had withheld any material information from the Revenue. The assessee was not bound to disclose that it had obtained an exemption from the competent authority under the Companies Act, 1956 from providing such details in its final accounts, balance sheets, etc. The Assessing Officer before finalising the assessment had not asked the assessee to furnish the details. The assessee disclosed all the primary facts necessary for assessment of its case to the Assessing Officer and it was not required to give any further assistance to the Assessing Officer by disclosure of other facts. The Assessing Officer on the basis of the facts disclosed to him did not doubt the genuineness of the transaction set up by the assessee which he could have done even at that stage on the basis of the facts which he already knew.*

*(iv) That whereas before the court the Department was urging that the assessee was guilty of non-disclosure of material facts, before the High Court the case of the Department was just the opposite. The Department could not be permitted to blow hot and cold at the same time.*

*(v) That in the notice dated March 31, 2015 there was no mention of any foreign entity. There was only mention of section 148. There was nothing in the reasons to indicate that the Department was intending to apply the extended period of 16 years. It was only after the assessee filed its reply to the reasons given, that in the order of rejection for the first time reference was made to the second proviso by the Department. This was not fair or proper procedure. If not in the first notice, at least at the time of furnishing the reasons the assessee should have been informed that the Department relied upon the second proviso. The assessee must be put to notice of all the provisions on which the Department relies upon. If the Department had issued a notice to the assessee stating that it relied upon the second proviso, the assessee would have had a chance to show that it was not deriving any income from any foreign asset or financial interest in any foreign entity, or that the asset did not belong to it or any other ground which may be available. The assessee could not be deprived of this chance while replying to the notice. The notice and reasons given thereafter did not conform to the principles of natural justice and the assessee did not get a proper and adequate opportunity to reply to the allegations which are now being relied upon by the Revenue. The notice issued to the assessee and the supporting reasons did not invoke provisions of the second proviso to section 147 of the Act and therefore at this stage the Department could not be permitted to take benefit of the second proviso.*

*[The court made it clear that it was not going into the merits of the case nor the question whether on facts of this case the Department could take*

*benefit of the second proviso. The Department was at liberty to issue fresh notice taking benefit of the second proviso if otherwise permissible under law.]*

*Decision of the High Court in* NEW DELHI TELEVISION LTD. *v.* DEPUTY CIT [2018] 405 ITR 132 (Delhi) *partly reversed*.

Cases referred to :

Calcutta Discount Co. Ltd. *v.* ITO [1961] 41 ITR 191 (SC) (para 32)

Clagett Brachi Co. Ltd. *v.* CIT [1989] 177 ITR 409 (SC) (para 21)

Ess Ess Kay Engineering Co. P. Ltd. *v.* CIT [2001] 247 ITR 818 (SC) (para 21)

Honda Siel Power Products Limited *v.* Deputy CIT [2012] 340 ITR 53 (Delhi) (para 27)

Mohinder Singh Gill *v.* Chief Election Commissioner [1978] 2 SCR 272 (para 39)

New Delhi Television Ltd. *v.* Deputy CIT [2018] 405 ITR 132 (Delhi) (para 9)

Phool Chand Bajrang Lal *v.* ITO [1993] 203 ITR 456 (SC) (para 21)

**Civil Appeal No. 1008 of 2020.**

Appeal from the judgment and order dated August 10, 2017 of the Delhi High Court in W. P. (C) No. 11638 of 2015. The judgment of the High Court is reported as *New Delhi Television Ltd.* v. *Deputy CIT* [2018] 405 ITR 132 (Delhi).

*Arvind P. Datar*, Senior Advocate, (*Sachit Jolly, Ms. Anuradha Dutt, Rohit Garg* and *Ms. B. Vijayalakshmi Menon*, Advocates, with him) for the appellant.

*Tushar Mehta,* Solicitor General and *Arijit Prasad*, Senior Advocate, (*Zoheb Hossain, Rajat Nair, Piyush Goyal* and *Mrs. Anil Katiyar*, Advocates, with them) for the respondent.

**JUDGMENT**

The judgment of the court was delivered by

1 DEEPAK GUPTA J.—The appellant-New Delhi Television Limited (hereinafter referred to as "the assessee") is an Indian company engaged in running television channels of various kinds. It has various foreign subsidiaries to which we shall refer in detail later on but we are concerned mainly with the subsidiary based in the United Kingdom (UK) named NDTV Network Plc., U.K. (hereinafter referred to as "NNPLC").

2 The assessee submitted a return for the financial year 2007-08 i.e., assessment year 2008-09 on September 29, 2008 declaring a loss. This

return was processed under section 143 of the Income-tax Act, 1961 (hereinafter referred to as "the Act"). The case was selected for scrutiny and notice under section 143(2) of the Act was issued and a notice under section 142(1) of the Act was also sent to the assessee. Thereafter, the case of the assessee was taken up for consideration and final assessment order was passed on August 3, 2012.

We are mainly concerned with that part of the assessment order which **3** relates to the issue of step-up coupon bonds amounting to US $ 100 million. These bonds were issued in July, 2007 through the Bank of New York for a period of 5 years. The case of the assessee is that NNPLC issued step-up coupon bonds of US $ 100 million which were arranged by Jeffries International and the funds were received by NNPLC through Bank of New York. The assessee had agreed to furnish corporate guarantee for this transaction. These bonds were subscribed to by various entities to whom we shall refer to in detail at a later stage. These bonds were to be redeemed at a premium of 7.5 per cent. after the expiry of the period of 5 years. However, these bonds were redeemed in advance at a discounted price of US $ 74.2 million in November, 2009.

The Assessing Officer held that NNPLC had virtually no financial worth, **4** it had no business of the name and therefore it could not be believed that it could have issued convertible bonds of US $ 100 million, unless the repayment along with interest was secured. This was secured only because of the assessee agreeing to furnish guarantee in this regard. Though the assessee had never actually issued such guarantee, the Assessing Officer was of the view that the subsidiary of the assessee could not have raised such a huge amount without having this assurance from the assessee. The transaction was of such a nature that the assessee should be required to maintain an arm's length from its subsidiary, meaning that it should be treated like a guarantee issued by any corporate guarantor in favour of some other corporate entity. The Assessing Officer did not doubt the validity of the transaction but imposed guarantee fee at the rate of 4.68 per cent. by treating it as a business transaction and added Rs. 18.72 crores to the income of the assessee, vide order dated August 3, 2012.

On March 31, 2015, the Revenue sent a notice to the assessee wherein it **5** was stated that the authority has reason to believe that net income chargeable to tax for the assessment year 2008-09 had escaped assessment within the meaning of section 148 of the Act. This notice did not give any reasons. The assessee then asked for the reasons and thereafter on August 4, 2015 reasons were supplied. The main reason given was that in the following assessment year, i.e., the assessment year 2009-10, the Assessing Officer

had proposed a substantial addition of Rs. 642 crores to the account of the assessee on account of monies raised by the assessee through its subsidiaries NDTV BV, The Netherlands, NDTV Networks BV, The Netherlands (NNBV), NDTV Networks International Holdings BV, The Netherlands (NNIH) and NNPLC. The assessee had raised its objection before the Dispute Resolution Panel (DRP) which came to the conclusion that all these transactions with the subsidiary companies in Netherlands were sham and bogus transactions and that these transactions were done with a view to get the undisclosed income, for which tax had not been paid, back to India by this circuitous round tripping.

6 The Assessing Officer relies upon the order of the DRP holding that there is reason to believe that the funds received by NNPLC were actually the funds of the assessee. It was specified that NNPLC had a capital of only Rs. 40 lakhs. It did not have any business activities in the United Kingdom except a postal address. Therefore, it appeared to the Assessing Officer that it was unnatural for anyone to make such a huge investment of $100 million in a virtually non-functioning company and thereafter get back only 72 per cent. of their original investment. According to the Assessing Officer "The natural inference could be that it was NDTV's own funds introduced in NNPLC in the garb of the impugned bonds". The details of the investors are given in this communication giving reasons. Mention has also been made of complaints received from a minority shareholder in which it is alleged that the money introduced in NNPLC was shifted to another subsidiary of the assessee in Mauritius from where it was taken to a subsidiary of the assessee in Mumbai and finally to the assessee. NNPLC itself was placed under liquidation on March 28, 2011. Therefore, the Assessing Officer was of the opinion that there were reasons to believe that the funds received by NNPLC were the funds of the assessee under a sham transaction and that the amount of Rs. 405.09 crores introduced into the books of NNPLC during the financial year 2007-08 corresponding to the assessment year 2008-09 through the transaction involving the step-up coupon convertible bonds pertains to the assessee. The last portion of the communication dated August 4, 2015 giving reasons to the assessee reads as follows :

> "7. In view of the above facts and circumstances of the case and considering the findings of the DRP holding the funds received by NNPLC as the funds of the assessee-New Delhi Television Limited under sham transactions, there is a reason to believe that the funds amounting to Rs. 405.09 crores introduced into the books of NNPLC during the financial year 2007-08 in the form of step up coupon

bonds pertain to the assessee-New Delhi Television Limited only. I have therefore reason to believe that the income of the assessee-New Delhi Television Limited for the assessment year 2008-09 amounting to at least Rs. 405.09 crores has escaped assessment. It is also recorded that the escapement is due to failure on the part of the assessee to disclose fully and truly all facts material for assessment."

7 The assessee filed the reply to the notice and reasons given, and claimed that there had been no failure on the part of the assessee to disclose fully and truly all material facts necessary to make an assessment. The assessee also claimed that the proceedings had been initiated on a mere change of opinion and there was no reason to believe. The assessee also claimed that the transaction of step-up bonds was a legal and valid transaction. In addition, it was claimed that the Assessing Officer had no valid reasons to believe that the income of the assessee had escaped assessment. According to the assessee the assessment officer had accepted the genuineness of the transaction wherein NNPLC, the subsidiary, had issued convertible bonds which had been subscribed by many entities. It was urged that the Assessing Officer had treated the transaction to be genuine by levying guarantee fees and adding it back to the income of the assessee. In the alternative, it was submitted that the notice had been issued beyond the period of limitation of 4 years. According to the assessee it had not withheld any material facts and, therefore, limitation of 6 years as applicable to the first proviso to section 147 would not apply.

8 The Assessing Officer did not accept these objections. The claim of the assessee was disposed of by the Assessing Officer vide order dated November 23, 2015 wherein the Assessing Officer held that there was non-disclosure of material facts by the assessee and the notice would be within limitation since NNPLC was a foreign entity and admittedly a subsidiary of the assessee and the income was being derived through this foreign entity. Hence, the case of the assessee would fall within the second proviso to section 147 of the Act and the extended period of 16 years would be applicable. The objections were accordingly rejected.

9 Aggrieved, the petitioner filed a writ petition in the High Court challenging the notice. The writ petition was dismissed on August 10, 2017[1]. Against this the assessee has filed the present appeal.

10 We have heard Shri Arvind P. Datar, learned senior counsel for the assessee, Shri Tushar Mehta, learned Solicitor General and Shri Zoheb Hossain, learned counsel appearing for the Revenue.

1. *New Delhi Television Ltd.* v. *Deputy CIT* [2018] 405 ITR 132 (Delhi).

**11** In our opinion, the following issues arise for consideration in this case :

"(i) Whether in the facts and circumstances of the case, it can be said that the Revenue had a valid reason to believe that undisclosed income had escaped assessment ?

(ii) Whether the assessee did not disclose fully and truly all material facts during the course of original assessment which led to the finalisation of the assessment order and undisclosed income escaping detection ?

(iii) Whether the notice dated March 31, 2015 along with reasons communicated on August 4, 2015 could be termed to be a notice invoking the provisions of the second proviso to section 147 of the Act ?"

**12** At the outset we may note that it has been strenuously urged on behalf of the assessee that its assessment was done under scrutiny procedure and a very detailed procedure was followed during the original assessment proceedings and all aspects of the case were noted by the Assessing Officer. That may be true, but merely the fact that the original assessment is a detailed one, cannot take away the powers of the Assessing Officer to issue notice under section 147 of the Act.

*Question No. 1*

**13** We would like to make it clear that we are not going into the merits of the allegations made against the assessee. At this stage we are only required to decide whether the Revenue has sufficient reasons to believe that undisclosed income of the assessee has escaped assessment and therefore there are grounds to issue notice. Obviously, during the assessment proceedings the assessee will have the right to place material on record to show that the transaction in question was a genuine transaction.

**14** It is trite law that an Assessing Officer can only reopen an assessment if he has "reason to believe" that undisclosed income has escaped assessment. Mere change of opinion of the Assessing Officer is not sufficient to meet the standard of "reason to believe". Relevant portion of section 147 reads as follows :

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 :

Provided further that nothing contained in the first proviso shall apply in a case where any income in relation to any asset (including financial interest in any entity) located outside India, chargeable to tax, has escaped assessment for any assessment year :

Provided also that the Assessing Officer may assess or reassess such income, other than the income involving matters which are the subject-matter 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 ;

(ba) where the assessee has failed to furnish a report in respect of any international transaction which he was so required under section 92E ;

(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.

(ca) where a return of income has not been furnished by the assessee or a return of income has been furnished by him and on the basis of information or document received from the prescribed income-tax authority, under sub-section (2) of section 133C, it is noticed by the Assessing Officer that the income of the assessee exceeds the maximum amount not chargeable to tax, or as the case may be, the assessee has understated the income or has claimed excessive loss, deduction, allowance or relief in the return ;

(d) where a person is found to have any asset (including financial interest in any entity) located outside India.

**15** The case of the assessee is that the transaction of step-up coupon bonds was scrutinised in great detail by the Assessing Officer before he passed the order of assessment dated August 3, 2012. According to the assessee there is an attempt on behalf of the Revenue to deliberately mix-up the transactions relating to the Netherlands subsidiary with the U.K. subsidiary. According to the assessee the order of the DRP for the assessment year 2009-10 is in two distinct compartments. While the DRP held the Netherlands' transactions of Rs. 642 crores to be a sham, the transaction of issuance of US$ 100 million convertible bonds was not questioned. Therefore, according to the assessee there was no fresh material before the Assessing Officer to have reason to believe that the undisclosed income of the assessee had escaped assessment.

**16** On behalf of the assessee it has been urged that once the transaction of step-up coupon bonds has been accepted to be correct, then the Revenue cannot reopen the same and doubt the genuineness of the transaction. We are not in agreement with the first part of the submission but we make it clear that we are not commenting on the genuineness of the transaction, which will be considered by the concerned Assessing Officer.

On the other hand, on behalf of the Revenue it is submitted that at the stage of issue of show-cause notice the Revenue only has to establish a tentative and prima facie view. At this stage, this court is not expected to go into the merits of the case but can only ascertain whether the Revenue has prima facie ground to show that it had reasons to believe that income has escaped assessment. It is further submitted that the scope of judicial review in such matters is very limited. It is also submitted that since the Revenue discovered fresh tangible material subsequent to the assessment order of August 3, 2012, it cannot be said that the Assessing Officer did not have reasons to believe that income had escaped assessment. **17**

The main issue is whether there was sufficient material before the Assessing Officer to take a prima facie view that income of the assessee had escaped assessment. The original order of assessment was passed on August 3, 2012. It was thereafter on December 31, 2013 that the DRP in the case of the assessment year 2009-10 raised doubts with regard to the corporate structure of the assessee and its subsidiaries. It was noted in the order of the DRP that certain shares of NNPLC had been acquired by Universal Studios International B.V., Netherlands, indirectly by subscribing to the shares of NNIH. As already noted above it was recorded in the reasons communicated on August 4, 2015 that NNPLC was not having any business activity in London. It had no fixed assets and was not even paying rent. Other than the fact that NNPLC was incorporated in the U.K., it had no other commercial business there. NNPLC had declared a loss of Rs. 8.34 crores for the relevant year. It was also noticed from the order of the Assessing Officer that the assessee is the parent company of NNPLC and it is the dictates of the assessee which are important for running NNPLC. **18**

Pursuant to the directions of the DRP, the Assessing Officer passed the final assessment order for the assessment year 2009-10 on February 21, 2014 which also disclosed similar facts. **19**

According to the Revenue tax evasion petitions were filed by the minority shareholders of the assessee-company on various dates, i.e., March 11, 2014, July 25, 2014, October 13, 2014 and March 11, 2015, which complaints describe in detail the communication between the assessee and the subsidiaries and also allegedly showed evidence of round tripping of the assessee's undisclosed income through a layer of subsidiaries which led to the issuance of the notice in question. **20**

Whether the facts which came to the knowledge of the assessment officer after the assessment proceedings for the relevant year were completed, could be taken into consideration for coming to the conclusion that there were reasons to believe that income had escaped assessment is the **21**

question that requires to be answered. Though a number of judgments have been cited in this behalf, we shall make reference to only a few. In *Clagett Brachi Co. Ltd.* v. *CIT*[1], this court held as follows[2] :

> "Two points have been urged before us by learned counsel for the assessee. It is contended that the Income-tax Officer has no jurisdiction to take proceedings under sections 147 and 148 of the Income-tax Act because the conditions prerequisite for making the reassessments were not satisfied. The reassessments were made with reference to clause (b) of section 147 of the Act, and apparently the Income-tax Officer proceeded on the basis that in consequence of information in his possession he had reason to believe that income chargeable to tax had escaped assessment for the two assessment years. From the material before us it appears that the Income-tax Officer came to realise that income had escaped assessment for the two assessment years when he was in the process of making assessment for a subsequent assessment year. While making that assessment he came to know from the documents pertaining to that assessment that the overhead expenses related to the entire business including the business as commission agents and were not confined to the business of purchase and sale. It is true, as the High Court has observed, that this information could have been acquired by the Income-tax Officer if he had exercised due diligence at the time of the original assessment itself. It does not appear, however, that the attention of the Income-tax Officer was directed by anything before him to the fact that the overhead expenses related to the entire business. The information derived by the Income-tax Officer evidently came into his possession when taking assessment proceedings for the subsequent year. In the circumstances, it cannot be doubted that the case falls within the terms of clause (b) of section 147 of the Act, and that, therefore, the High Court is right in holding against the assessee."

In *Phool Chand Bajrang Lal* v. *ITO*[3], this court held as follows[4] :

> "Acquiring fresh information, specific in nature and reliable in character, relating to the concluded assessment which goes to expose the falsity of the statement made by the assessee at the time of original assessment is different from drawing a fresh inference from the same facts and material which was available with the

1. [1989] 177 ITR 409 (SC) ; [1989] Supp. (2) SCC 182
2. Page 413 of 177 ITR.
3. [1993] 203 ITR 456 (SC) ; [1993] 4 SCC 77.
4. Page 473 of 203 ITR.

Income-tax Officer at the time of original assessment proceedings. The two situations are distinct and different. Thus, where the transaction itself on the basis of subsequent information, is found to be a bogus transaction, the mere disclosure of that transaction at the time of original assessment proceedings, cannot be said to be disclosure of the 'true' and 'full' facts in the case and the Income-tax Officer would have the jurisdiction to reopen the concluded assessment in such a case. It is correct that the assessing authority could have deferred the completion of the original assessment proceedings for further enquiry and investigation into the genuineness to the loan transaction but in our opinion his failure to do so and complete the original assessment proceedings would not take away his jurisdiction to act under section 147 of the Act, on receipt of the information subsequently. The subsequent information on the basis of which the Income-tax Officer acquired reasons to believe that income chargeable to tax had escaped assessment on account of the omission of the assessee to make a full and true disclosure of the primary facts was relevant, reliable and specific. It was not at all vague or non-specific."

In *Ess Ess Kay Engineering Co. P. Ltd.* v. *CIT*[1], this court held as follows :

"This is a case of reopening. We have perused the documents. We find there was material on the basis of which the Income-tax Officer could proceed to reopen the case. It is not a case of mere change of opinion. We are not inclined to interfere with the decision of the High Court merely because the case of the assessee was accepted as correct in the original assessment for this assessment year. It does not preclude the Income-tax Officer from reopening the assessment of an earlier year on the basis of his findings of fact made on the basis of fresh materials in the course of assessment of the next assessment year. The appeal is dismissed. No order as to costs."

A perusal of the aforesaid judgments clearly shows that subsequent facts **22**
which come to the knowledge of the Assessing Officer can be taken into account to decide whether the assessment proceedings should be reopened or not. Information which comes to the notice of the Assessing Officer during proceedings for subsequent assessment years can definitely form tangible material to invoke powers vested with the Assessing Officer under section 147 of the Act.

1. [2001] 247 ITR 818 (SC) ; [2001] 10 SCC 189.

**23** The material disclosed in the assessment proceedings for the subsequent years as well as the material placed on record by the minority shareholders form the basis for taking action under section 147 of the Act. At the stage of issuance of notice, the Assessing Officer is to only form a prima facie view. In our opinion the material disclosed in assessment proceedings for subsequent years was sufficient to form such a view. We accordingly hold that there were reasons to believe that income had escaped assessment in this case. Question No. 1 is answered accordingly.

*Question No. 2*

**24** Coming to the second question as to whether there was failure on the part of the assessee to make a full and true disclosure of all the relevant facts. The case of the assessee is that it had disclosed all facts which were required to be disclosed.

**25** The Revenue has placed reliance on certain complaints made by the minority shareholders and it is alleged that those complaints reveal that the assessee was indulging in round tripping of its funds. According to the Revenue the material disclosed in these complaints clearly shows that the assessee is guilty of creating a network of shell companies with a view to transfer its untaxed income in India to entities abroad and then bring it back to India thereby avoiding taxation. We make it clear that we are not going into this aspect of the matter because those complaints have not seen the light of the day either before the High Court or this court and, therefore, it would be unfair to the assessee if we rely upon such material which the assessee has not been confronted with.

**26** Even before the assessment order was passed on August 3, 2012, the Assessing Officer was aware of the entities which had subscribed to the convertible bonds. This is apparent from the communication dated April 8, 2011. The case of the Revenue is that the assessee did not disclose the amount subscribed by each of the entities and furthermore the management structure of these companies. We are not in agreement with this submission of the Revenue. It is apparent from the records of the case that the Revenue was aware of the entities which subscribed to the convertible bonds. It has been urged that these are bogus companies, but we are not concerned with that at this stage. The issue before us is whether the Revenue can take the benefit of the extended period of limitation of 6 years for initiating proceedings under the first proviso to section 147 of the Act. This can only be done if the Revenue can show that the assessee had failed to disclose fully and truly all material facts necessary for its assessment. The assessee, in our view had disclosed all the facts it was bound to disclose. If

the Revenue wanted to investigate the matter further at that stage it could have easily directed the assessee to furnish more facts.

27 The High Court held that there was no "true and fair disclosure" in view of the law laid down by this court in *Phool Chand's* case (supra), and the judgment of the Delhi High Court in *Honda Siel Power Products Limited* v. *Deputy CIT*[1]. We have already referred to the judgment in *Phool Chand's* case (supra), wherein it was held that where the transaction of a particular assessment year is found to be a bogus transaction, the disclosures made could not be said to be all "true" and "full". Relying upon the said judgment the High Court held that merely because the transaction of convertible bonds was disclosed at the time of original assessment does not mean that there is true and full disclosure of facts.

28 We are unable to agree with this reasoning given by the High Court. The assessee as mentioned above made a disclosure about having agreed to stand guarantee for the transaction by NNPLC and it had also disclosed the factum of the issuance of convertible bonds and their redemption. The income, if any, arose because of the redemption at a discounted price. This was an event which took place subsequent to the assessment year in question though it may be income for the assessment year. As we have observed above, all relevant facts were duly within the knowledge of the Assessing Officer. The Assessing Officer knew who were the entities who had subscribed to other convertible bonds and in other proceedings relating to the subsidiaries the same Assessing Officer had knowledge of addresses and the consideration paid by each of the bondholders as is apparent from assessment orders dated August 3, 2012 passed in the cases of M/s. NDTV Labs Ltd. and M/s. NDTV Lifestyle Ltd. Therefore, in our opinion there was full and true disclosure of all material facts necessary for its assessment by the assessee.

29 The fact that step-up coupon bonds for US $ 100 million were issued by NNPLC was disclosed ; who were the entities which subscribed to the bonds was disclosed ; and the fact that the bonds were discounted at a lower rate was also disclosed before the assessment was finalised. This transaction was accepted by the Assessing Officer and it was clearly held that the assessee was only liable to receive a guarantee fees on the same which was added to its income. Without saying anything further on merits of the transaction we are of the view that it cannot be said that the assessee had withheld any material information from the Revenue.

30 According to the Revenue the assessee to avoid detection of the actual source of funds of its subsidiaries did not disclose the details of the

1. [2012] 340 ITR 53 (Delhi).

subsidiaries in its final accounts, balance-sheets, and profit and loss account for the relevant period as was mandatory under the provisions of the Indian Companies Act, 1956. It is not disputed that the assessee had obtained an exemption from the competent authority under the Companies Act, 1956 from providing such details in its final accounts, balance-sheets, etc. As such it cannot be said that the assessee was bound to disclose this to the Assessing Officer. The Assessing Officer before finalising the assessment of August 3, 2012 had never asked the assessee to furnish the details.

**31** The Revenue now has come up with the plea that certain documents were not supplied but according to us all these documents cannot be said to be documents which the assessee was bound to disclose at the time of assessment. The main ground raised by the Revenue is that the assessee did not disclose as to who had subscribed what amount and what was its relationship with the assessee. As far as the first part is concerned it does not appear to be correct. There is material on record to show that on April 8, 2011 NNPLC had sent a communication to the Deputy Director of Income-tax (Investigation), wherein it had not only disclosed the names of all the bondholders but also their addresses ; number of bonds along with the total consideration received. This chart forms part of the assessment orders dated August 3, 2012 in the case of M/s. NDTV Labs Ltd. and M/s. NDTV Lifestyle Ltd. The said two assessment orders were passed by the same officer who had passed the assessment order in the case of the assessee on the same date itself. Therefore, the entire material was available with the Revenue.

**32** A number of decisions have been cited as to what is meant by true and full disclosure. It is not necessary to multiply decisions, as law in this regard has been succinctly laid down by a Constitution Bench of this court in *Calcutta Discount Co. Ltd.* v. *ITO*[1], wherein it was held as follows[2] :—

> ". . . The words used are 'omission or failure to disclose fully and truly all material facts necessary for his assessment for that year'. It postulates a duty on every assessee to disclose fully and truly all material facts necessary for his assessment. What facts are material, and necessary for assessment will differ from case to case. In every assessment proceeding, the assessing authority will, for the purpose of computing or determining the proper tax due from an assessee, require to know all the facts which help him in coming to the correct conclusion. From the primary facts in his possession, whether on

1. [1961] 41 ITR 191 (SC) ; AIR 1961 SC 372.
2. Page 200 of 41 ITR.

disclosure by the assessee, or discovered by him on the basis of the facts disclosed, or otherwise, the assessing authority has to draw inferences as regards certain other facts ; and ultimately, from the primary facts and the further facts inferred from them, the authority has to draw the proper legal inferences, and ascertain on a correct interpretation of the taxing enactment, the proper tax leviable. Thus, when a question arises whether certain income received by an assessee is capital receipt, or revenue receipt, the assessing authority has to find out what primary facts have been proved, what other facts can be inferred from them, and taking all these together, to decide what the legal inference should be.

There can be no doubt that the duty of disclosing all the primary facts relevant to the decision of the question before the assessing authority lies on the assessee. To meet a possible contention that when some account books or other evidence has been produced, there is no duty on the assessee to disclose further facts, which on due diligence, the Income-tax Officer might have discovered, the Legislature has put in the *Explanation*, which has been set out above. In view of the *Explanation*, it will not be open to the assessee to say, for example — 'I have produced the account books and the documents : You, the Assessing Officer examine them, and find out the facts necessary for your purpose : My duty is done with disclosing these account-books and the documents.' His omission to bring to the assessing authority's attention these particular items in the account books, or the particular portions of the documents, which are relevant, will amount to 'omission to disclose fully and truly all material facts necessary for his assessment'. Nor will he be able to contend successfully that by disclosing certain evidence, he should be deemed to have disclosed other evidence, which might have been discovered by the assessing authority if he had pursued investigation on the basis of what has been disclosed. The *Explanation* to the section, gives a quietus to all such contentions ; and the position remains that so far as primary facts are concerned, it is the assessee's duty to disclose all of them — including particular entries in account books, particular portions of documents and documents, and other evidence, which could have been discovered by the assessing authority, from the documents and other evidence disclosed.

Does the duty however extend beyond the full and truthful disclosure of all primary facts ? In our opinion, the answer to this question must be in the negative. Once all the primary facts are before the

assessing authority, he requires no further assistance by way of disclosure. It is for him to decide what inferences of facts can be reasonably drawn and what legal inferences have ultimately to be drawn. It is not for somebody else — far less the assessee — to tell the assessing authority what inferences, whether of facts or law should be drawn. Indeed, when it is remembered that people often differ as regards what inferences should be drawn from given facts, it will be meaningless to demand that the assessee must disclose what inferences — whether of facts or law — he would draw from the primary facts.

If from primary facts more inferences than one could be drawn, it would not be possible to say that the assessee should have drawn any particular inference and communicated it to the assessing authority. How could an assessee be charged with failure to communicate an inference, which he might or might not have drawn ?"

A careful analysis of this judgment indicates that the Constitution Bench held that it is the duty of the assessee to disclose fully and truly all material facts which it termed as primary facts. Non-disclosure of other facts which may be termed as secondary facts is not necessary. In the light of the above law, we shall deal with the facts of the present case.

**33** In our view the assessee disclosed all the primary facts necessary for assessment of its case to the Assessing Officer. What the Revenue urges is that the assessee did not make a full and true disclosure of certain other facts. We are of the view that the assessee had disclosed all primary facts before the Assessing Officer and it was not required to give any further assistance to the Assessing Officer by disclosure of other facts. It was for the Assessing Officer at this stage to decide what inference should be drawn from the facts of the case. In the present case the Assessing Officer on the basis of the facts disclosed to him did not doubt the genuineness of the transaction set up by the assessee. This the Assessing Officer could have done even at that stage on the basis of the facts which he already knew. The other facts relied upon by the Revenue are the proceedings before the DRP and facts subsequent to the assessment order, and we have already dealt with the same while deciding issue No. 1. However, that cannot lead to the conclusion that there is non-disclosure of true and material facts by the assessee.

**34** It is interesting to note that whereas before this court the Revenue is strenuously urging that the assessee is guilty of non-disclosure of material facts, before the High Court the case of the Revenue was just opposite. We may quote a portion of the counter-affidavit filed by the Revenue in

response to the writ petition filed by the assessee before the High Court which reads as follows :-

> ". . . It is evident from these facts that the second proviso to section 147 is clearly attracted in this case and the first proviso to section 147 is not applicable to the facts of this case, i.e., in this case, the only requirement to reopen assessment under section 147 was that the Assessing Officer has reason to believe that any income chargeable to tax has escaped assessment. The second condition that the income should have escaped assessment due to failure on the part of the assessee to disclose fully and truly all material facts necessary for making assessment is not relevant to decide the issue before the hon'ble court."

This submission has been repeated a number of times in the counter-affidavit. Therefore, in our opinion the Revenue cannot now turn around and urge that the assessee is guilty of non-disclosure of facts. We are also of the view that the Revenue could not be permitted to blow hot and cold at the same time.

We are clearly of the view that the Revenue in view of its counter-affi- **35**
davit before the High Court that it was not relying upon the non-disclosure of facts by the assessee could not have been permitted to orally urge the same. Even otherwise we find that the assessee had fully and truly disclosed all material facts necessary for its assessment and, therefore, the Revenue cannot take the benefit of the extended period of limitation of 6 years. We answer question No. 2 accordingly.

*Question No. 3*

It is urged before this court by the Revenue that in terms of second pro- **36**
viso to section 147 of the Act read with section 149(1)(c) of the Act, the limitation period would be 16 years since the assessee has derived income from a foreign entity. We may make specific reference to the second proviso and *Explanation 2(d)* which reads as follows :

> "Provided further that nothing contained in the first proviso shall apply in a case where any income in relation to any asset (including financial interest in any entity) located outside India, chargeable to tax, has escaped assessment for any assessment year :
>
> *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 :— . . .
>
> (d) where a person is found to have any asset (including financial interest in any entity) located outside India."

**37** On behalf of the assessee it has been urged that no income was derived from the foreign entity and a loan cannot be termed to be an asset or an income and it is submitted that the notice cannot be said to have been issued under the second proviso.

**38** In this regard we may make reference to the notice dated March 31, 2015. The notice is conspicuously silent with regard to the second proviso. It does not rely upon the second proviso and basically relies on the provisions of section 148 of the Act. The reasons communicated to the assessee on August 4, 2015 mention "reason to believe" and non-disclosure of material facts by the assessee. There is no case set up in relation to the second proviso either in the notice or even in the reasons supplied on August 4, 2015 with regard to the notice. It is only while rejecting the objections of the assessee that reference has been made to the second proviso in the order of disposal of objections dated November 23, 2015.

**39** The High Court relied upon the judgment in *Mohinder Singh Gill* v. *Chief Election Commissioner*[1] and came to the conclusion that the Revenue cannot rely upon the second proviso because the notice was silent in this regard. However, the High Court held that the assessee was guilty of non-disclosure of material facts. We have already held that in our view the assessee was not guilty of non-disclosure of material facts. The Revenue has not challenged the judgment of the High Court in so far as this finding against it is concerned but the Revenue is entitled to defend the petition even on a ground which may have been decided against it by the High Court.

**40** On behalf of the Revenue it is urged that mere non-naming of the second proviso in the notice does not help the assessee. It has been urged that even if the source of power to issue notice has been wrongly mentioned, but all relevant facts were mentioned, then the notice can be said to be notice under the provision which empowers the Revenue to issue such notice. There can be no quarrel with this proposition of law. However, the noticee or the assessee should not be prejudiced or be taken by surprise. The uncontroverted fact is that in the notice dated March 31, 2015 there is no mention of any foreign entity. There is only mention of section 148. Even after the assessee specifically asked for reasons, the Revenue only relied upon the facts to show that there was reason to believe that income has escaped assessment and this escapement was due to the non-disclosure of material facts. There is nothing in the reasons to indicate that the Revenue was intending to apply the extended period of 16 years. It is only after the assessee filed its reply to the reasons given, that in the order of

1. [1978] 2 SCR 272.

rejection for the first time reference was made to the second proviso by the Revenue.

In our view this is not a fair or proper procedure. If not in the first notice, **41** at least at the time of furnishing the reasons the assessee should have been informed that the Revenue relied upon the second proviso. The assessee must be put to notice of all the provisions on which the Revenue relies upon. At the risk of repetition, we reiterate that we are not going into the merits of the case but in case the Revenue had issued a notice to the assessee stating that it relies upon the second proviso, the assessee would have had a chance to show that it was not deriving any income from any foreign asset or financial interest in any foreign entity, or that the asset did not belong to it or any other ground which may be available. The assessee cannot be deprived of this chance while replying to the notice.

Therefore, even if we do not fall back on the reason given by the High **42** Court that the Revenue cannot take a fresh ground, we are clearly of the view that the notice and reasons given thereafter do not conform to the principles of natural justice and the assessee did not get a proper and adequate opportunity to reply to the allegations which are now being relied upon by the Revenue.

If the Revenue is to rely upon the second proviso and wanted to urge **43** that the limitation of 16 years would apply, then in our opinion in the notice or at least in the reasons in support of the notice, the assessee should have been put to notice that the Revenue relies upon the second proviso. The assessee could not be taken by surprise at the stage of rejection of its objections or at the stage of proceedings before the High Court that the notice is to be treated as a notice invoking the provisions of the second proviso to section 147 of the Act. Accordingly, we answer the third question by holding that the notice issued to the assessee and the supporting reasons did not invoke the provisions of the second proviso to section 147 of the Act and therefore at this stage the Revenue cannot be permitted to take the benefit of the second proviso.

*Conclusion*

We accordingly allow the appeal by holding that the notice issued to the **44** assessee shows sufficient reasons to believe on the part of the Assessing Officer to reopen the assessment but since the Revenue has failed to show non-disclosure of facts the notice having been issued after a period of 4 years is required to be quashed. Having held so, we make it clear that we have not expressed any opinion on whether on the facts of this case the Revenue could take benefit of the second proviso or not. Therefore, the Revenue may issue fresh notice taking the benefit of the second proviso if

otherwise permissible under law. We make it clear that both the parties shall be at liberty to raise all contentions with regard to the validity of such notice. All pending application(s) shall stand(s) disposed of.

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**[2020] 424 ITR 630 (SC)**

[IN THE SUPREME COURT OF INDIA]

## YUM! RESTAURANTS (MARKETING) PRIVATE LIMITED

*v.*

## COMMISSIONER OF INCOME-TAX

**A. M. KHANWILKAR** and **DINESH MAHESHWARI** JJ.

April 24, 2020.

**SS ▶ ITA 1961, s 2(24)**
**AY ▶ 2001-02**
**HF ▶ Department**

INCOME—PRINCIPLE OF MUTUALITY—TESTS—ASSESSEE INCORPORATED AS FULLY OWNED SUBSIDIARY OF PARENT COMPANY WITH APPROVAL FROM SECRETARIAT FOR INDUSTRIAL ASSISTANCE—APPROVAL SUBJECT TO CONDITIONS THAT IT WOULD OPERATE ON NON-PROFIT BASIS ON PRINCIPLES OF MUTUALITY—ASSESSEE ENTERING INTO TRIPARTITE OPERATING AGREEMENT WITH PARENT COMPANY AND ITS FRANCHISEES—ASSESSEE RECEIVING FIXED CONTRIBUTIONS OF 5 PER CENT. OF GROSS SALES FROM FRANCHISEES FOR ADVERTISING, MARKETING AND PROMOTIONAL ACTIVITIES FOR MUTUAL BENEFIT OF PARENT COMPANY AND FRANCHISEES—ASSESSEE REALISING MONEY BOTH FROM MEMBERS AS WELL AS NON-MEMBERS—RECEIPT OF MONEY FROM OUTSIDE ENTITY WITHOUT AFFORDING IT RIGHT TO SHARE IN SURPLUS CONTRARY TO PRINCIPLES OF MUTUALITY—MANAGEMENT OF ASSESSEE UNDER FULL AND ABSOLUTE CONTROL OF PARENT COMPANY—PARENT COMPANY ENJOYING OVERRIDING DISCRETION TO DETRIMENT OF FRANCHISEES BOTH IN MATTERS OF CONTRIBUTION AND MANAGEMENT—FRANCHISEES HAVING NO "ENTITLEMENT" OR "RIGHT" ON SURPLUS—DERIVATION OF GAINS OR PROFITS OUT OF INPUTS SUPPLIED BY OTHERS—NO OBLIGATION ON ASSESSEE TO SPEND CONTRIBUTIONS FOR BENEFIT OF CONTRIBUTORS—ASSESSEE NOT HOLDING AMOUNT UNDER ANY IMPLIED TRUST FOR FRANCHISEES—PURPORTED MUTUAL CONCERN UNDERTOOK COMMERCIAL VENTURE WHEREIN CONTRIBUTIONS WERE ACCEPTED BOTH FROM MEMBERS AS WELL AS NON-MEMBERS—CONDITIONS OF APPROVAL VIOLATED—ASSESSEE NOT A MUTUAL CONCERN—NO CASE FOR EXEMPTION—INCOME-TAX ACT, 1961, S. 2(24).

*The doctrine of mutuality traces its origin to the basic principle that a man cannot engage in business with himself. For that reason, it is deemed at law that if the identity of the seller and the buyer, or the vendor and the consumer, or the contributor and the participator is marked by oneness, a profit motive cannot be attached to such a venture. Thus, for the lack of a profit motive, the excess of income over the expenditure or the "surplus" remaining in the hands of such a venture cannot be regarded as "income" taxable under the Income-tax Act, 1961. What is taxable under the Act is "income" or "profits" or "gains" as they accrue to a person in his dealings with other party or parties that do not share the same identity with the assessee. For income, there is an underlying exchange of a commercial nature between two different entities.*

*The three conditions or tests to prove the existence of mutuality are : (i) identity of the contributors to the fund and the recipients from the fund ; (ii) treatment of the company, though incorporated as a mere entity for the convenience of the members and policy holders, in other words, as an instrument obedient to their mandate ; and (iii) impossibility that contributors should derive profits from contributions made by themselves to a fund which could only be expended or returned to themselves.*

*The first element involves the test of commonality of identity between the members or participators in the mutual concern and the beneficiaries thereof. This limb requires that no person ought to contribute to the common fund without having the entitlement to participate as a beneficiary in the surplus thereof. Conversely, no person ought to participate as a beneficiary without first having been a contributor or a member of the class of contributors to the common fund. Common identity signifies that the class of members should stay intact as the transaction progresses from the stage of contributions to that of returns and surplus. It must manifest uniformity in the class of participants in the transaction. The moment such a transaction opens itself to non-members, either in the contribution or the surplus, the uniformity of identity is impaired and the transaction assumes the taint of a commercial transaction. The doctrine of mutuality does not prohibit the inclusion or exclusion of new members. What is prohibited is the infusion of a participant in the transaction who does not become a "member" of the common fund, at par with other members, and yet participates either in the contribution or surplus without subjecting itself to mutual rights and obligations. The principle of common identity prohibits any one-dimensional alteration in the nature of participation in the mutual fund as the transaction fructifies. Any such alteration would lead to the non-uniform participation of an external element or*

*entity in the transaction, thereby opening the scope for a manifest or latent profit-based dealing in the transaction with parties outside the closed circuit of members. It would be amenable to income-tax in terms of section 2(24) of the Act.*

*Coterminous with the requirement of common identity, the law also contemplates a completeness of identity between the contributors and participators. The theory of completeness of identity presupposes the contributors and participators to be two separate classes, but there is oneness or equality in the matter of sharing of surplus or profits. This is to ensure that there is no interference of any alien commercial entity in the transaction. With the interference of any alien entity, the idea of conducting business with oneself is defeated and any profits or gains accruing therefrom become subject to tax liability.*

*The factual determination of whether an entity is a mutual concern on a case to case basis poses a complex issue that requires deeper examination. In order to determine the breach in mutuality, the court is well within its powers to go beyond the periphery of the concern and undertake an examination akin to the lifting of the veil in order to discern the real nature thereof.*

*The members of a financial concern exercise mutual control over its management without the scope of prejudicial exercise of power by one class of members over the others. This is the quintessence for the existence of a mutual concern. Literally understood, the word "mutual" points towards reciprocity and a mutual arrangement is one in which the members and parties have reciprocal rights or understanding or arrangement. An arrangement wherein one member is subjected to the absolute discretion of another, in such a manner that the entire liability may fall upon one whereas benefits are reaped by all, is an antithesis to the mutual character in the eyes of law.*

*Although every member of the mutual concern might not be required to contribute to the common pool at all times, this does not mean that one member cannot be made to contribute under any pretext whatsoever. That would amount to the grant of an overriding position to a member in the mutual agreement, extending even to overruling requests for contribution from other members for mutual necessity. It is this all-pervasive overriding position of one member over the others that negates the effect of mutuality. There is a fine line of distinction between absence of obligation and presence of overriding discretion. In a mutual concern, it is no doubt true that an obligation to pay may or may not be there, but in the same breath, it is equally true that an overriding discretion of one member over others cannot be sustained, in order*

*to preserve the real essence of mutuality wherein members contribute for the mutual benefit of all and not of one at the cost of others.*

*In order to qualify as a mutual concern, the contributors to the common fund either acquire a right to participate in the surplus or an entitlement to get back the remaining proportion of their respective contributions. The raison d'etre behind the refund of surplus to the contributors or mandatory utilisation thereof in the subsequent assessment year is to reduce their burden of contribution in the next year proportionate to the surplus remaining from the previous year. Thus, the fulfilment of this condition becomes essential.*

*The doctrine of mutuality, in principle, entails that there should not be any profit earning motive, either directly or indirectly. The third test of mutuality requires that the purported mutual operations must be marked by an impossibility of profits.*

*The exemption granted to a mutual concern is premised on the assumption that the concern is being run for the mutual benefit of the contributors and the contributions made by the members ought to be directed in that direction.*

*The doctrine of mutuality bestows a special status to qualify for exemption from tax liability. It is a settled proposition of law that exemptions are to be put to strict interpretation.*

*The assessee-company was incorporated by YRIPL as its fully owned subsidiary after having obtained approval from the Secretariat for Industrial Assistance for the purpose of economisation of the cost of advertising and promotion of the franchisees according to their needs. The approval was granted subject to certain conditions as regards the functioning of the assessee, whereby it was obligated to operate on a non-profit basis on the principles of mutuality. In furtherance of the approval, the assessee entered into a tripartite operating agreement with YRIPL and its franchisees, whereunder the assessee received fixed contributions to the extent of 5 per cent. of gross sales for the proper conduct of the advertising, marketing and promotional activities for the mutual benefit of the parent company and the franchisees. For the assessment year 2001-02, the assessee filed its returns showing nil income on the principle of mutuality. This was not accepted by the Assessing Officer, the Commissioner (Appeals) or the Tribunal on the finding that the essential ingredients of the doctrine of mutuality were missing. The consistent opinion recorded by the three forums was approved in appeal by the High Court. On further appeal :*

Held, *dismissing the appeal, (i) that P was a contributor to the common pool of funds but did not participate in the surplus as a beneficiary, because it was not a member of the purported mutual concern as the tripartite*

*agreement and the terms of the SIA approval permitted only franchisees to become members of the mutual concern. P was not a franchisee and thus, could not participate in the surplus. P did not enjoy any right of participation in the surplus or any right to receive back the surplus which are mandatory ingredients to sustain the principle of mutuality. Moreover, the tripartite agreement required the assessee to constitute a separate brand fund for each franchisee. Since no brand fund had been constituted for P, it did not become a part of the tripartite mutual arrangement so as to qualify as a beneficiary of the mutual operations. For any amount received by the assessee to be treated as an advertising contribution, it must be paid by a franchisee, that too pursuant to a prior franchisee agreement to that effect. There was no such franchisee agreement with P and therefore, the amounts received from P could not be viewed as advertising contributions "from a member of the mutual undertaking". Therefore, the assessee was realising money both from members as well as non-members in the course of the same activity. Such operations were antithetical to mutuality. Even if any remote or indirect benefit was being reaped by P, that could not be said to be in lieu of its being a member of the purported mutual concern. The surplus of a mutual operation is meant to be utilised by the members of the mutual concern as members enjoy a proximate connection with the mutual operation. Non-members, including P, stood on a different footing and had no proximate connection with the affairs of the mutual concern.*

*(ii) That the receipt of money from an outside entity without affording it the right to have a share in the surplus also contravened the other two conditions for the existence of mutuality, i. e., impossibility of profits and obedience to the mandate. The mandate of the assessee was laid down in the SIA approval wherein the twin conditions of mutuality and non-profiteering were envisioned as the sine qua non for the functioning of the assessee. The contributions made by P tainted the operations of the assessee with commerciality and concomitantly contravened the prerequisites of mutuality and non-profiteering.*

*(iii) That the mutuality and non-profiteering character of a concern were to be determined in the light of its actual working structure and the factum of corporation or incorporation or the form in which it is clothed was immaterial. According to the terms of the SIA approval, YRIPL and the franchisees were equally obligated to make contributions of a fixed percentage to the assessee. This requirement was incorporated as a precondition for the grant of permission to operate as a mutual concern. However, the tripartite agreement made it discretionary upon YRIPL to contribute to the common*

*pool, thereby putting it at a higher pedestal than the franchisees. Thus the tripartite agreement was not in conformity with the terms of the approval. Furthermore, the management of the assessee was under the full and absolute control of its parent company YRIPL and the participation of the franchisees in the management of the assessee was again subject to approval by YRIPL. The net effect was to render the preconditions for the grant of approval otiose. YRIPL and the franchisees stood on two substantially different footings. Moreover, even upon request for the grant of funds by the assessee, YRIPL was not bound to accede to the request and enjoyed a "sole and absolute" discretion to decide against such request.*

*(iv) That YRIPL enjoyed an overriding discretion to the detriment of the franchisees of the purported undertaking, both in matters of contribution and management.*

*(v) That the franchisees did not enjoy any "entitlement" or "right" on the surplus remaining after the operations had been carried out for a given assessment year. The assessee might refund the surplus subject to the approval of its board of directors. This implied that the franchisees or contributors could not claim a refund of their remaining amount as a matter of right. Even if any surplus remained in a given assessment year, it was unlikely to reduce the liability of the franchisees in the following year as their liability to the extent of 5 per cent. was fixed and non-negotiable, irrespective of whether any funds were in surplus in the previous year. The only entity that could derive any benefit from the surplus funds was YRIPL, i.e., the parent company. This was antithetical to the third test of mutuality.*

*(vi) That the dispensation predicated in the tripartite agreement may entail in a situation where YRIPL would not contribute even a single penny to the common pool and yet be able to derive profits in the form of royalties out of the purported mutual operations, created from the fixed 5 per cent. contribution made by the franchisees. This would be nothing short of derivation of gains or profits out of inputs supplied by others. That was violative of the basic essence of mutuality. Furthermore, the tripartite agreement relieved the assessee from any specific obligation of spending the amounts received by way of contributions for the benefit of the contributors. The assessee did not hold such amount under any implied trust for the franchisees. A priori, it must follow that the assessee had acted in contravention of the terms of approval. Notably, the SIA approval or Government approval was not only a binding document but also a conditional document with a defined set of preconditions for the functioning of the assessee as a mutual concern. The SIA approval categorically was subject to the terms and conditions specified therein and*

*any contravention thereof would be infraction of the mandate of the Government approval.*

*(vii) That the assessee's argument that no fixed percentage of contribution could be imputed upon YRIPL as it did not operate any restaurant directly and thus, the actual volume of sales could not be determined was not tenable as YRIPL received a fixed percentage of royalty from the franchisees on the sales. If the franchisees could be obligated with a fixed percentage of contribution, there was no reason why the same obligation ought not to apply to YRIPL. The assessee was formed to manage the business on behalf of the holding company. In its true form, it was not contemplated as a non-business concern because operations integral to the functioning of a business were entrusted to it.*

*(viii) The assessee having failed to fulfil the stipulations and to prove the existence of mutuality, the question of extending exemption from tax liability to the assessee did not arise. The purported mutual concern undertook a commercial venture wherein contributions were accepted both from the members as well as non-members. Moreover, one member was vested with a myriad set of powers to control the functioning and interests of other members (franchisees), even to their detriment. Such an assimilation was not a case of ordinary social intercourse devoid of commerciality.*

*(ix) That the question of diversion by overriding title was neither framed nor agitated in the appeal before the High Court or before the court and neither the Tribunal nor the High Court had dealt with that plea. The rectification application raising that ground was still undecided and stated to be pending before the Tribunal. [It was open to the assessee to pursue the rectification application, if so advised.]*

CIT *v.* BANKIPUR CLUB LTD. [1997] 226 ITR 97 (SC), BANGALORE CLUB *v.* CIT [2013] 350 ITR 509 (SC), ENGLISH AND SCOTTISH JOINT COOPERATIVE WHOLESALE SOCIETY LTD. *v.* COMMR. OF AGRL. I. T. [1948] 16 ITR 270 (PC) *and* CIT *v.* ROYAL WESTERN INDIA TURF CLUB LTD. [1953] 24 ITR 551 (SC) *relied on.*

*Decision of the Delhi High Court* (printed below) *affirmed.*

Cases referred to :

Associated Power Co. Ltd. *v.* CIT [1996] 218 ITR 195 (SC) (para 38)

Bangalore Club *v.* CIT [2013] 350 ITR 509 (SC) (para 15)

CIT *v.* Bankipur Club Ltd. [1997] 226 ITR 97 (SC) (para 14)

CIT *v.* Royal Western India Turf Club Ltd. [1953] 24 ITR 551 (SC) (para 16)

CIT *v.* Sitaldas Tirathdas [1961] 41 ITR 367 (SC) (para 38)

CIT *v.* Travancore Sugars and Chemicals Ltd. [1973] 88 ITR 1 (SC) (para 38)

Dalmia Cement Ltd. *v.* CIT [1999] 237 ITR 617 (SC) (para 38)

English and Scottish Joint Co-operative Wholesale Society Ltd. *v.* Commr. of Agrl. I. T. [1948] 16 ITR 270 (PC) (para 16)

New York Life Insurance Co. *v.* Styles (Surveyor of Taxes) [1889] 2 TC 460 (para 15)

**Civil Appeal No. 2847 of 2010.**

Appeal from the judgment and order dated April 1, 2009 of the Delhi High Court in I. T. A. No. 1433 of 2008. The judgment of the High Court (VIKRAMAJIT SEN and RAJIV SHAKDHER JJ.) ran as follows :

"JUDGMENT

1. This is an appeal preferred by the assessee-company under section 260A of the Income-tax Act, 1961 (hereinafter referred to as the 'Act') against the judgment dated January 31, 2008 passed by the Income-tax Appellate Tribunal (hereinafter referred to as the "Tribunal") in I. T. A. No. 3235/Del/2005 pertaining to assessment year 2001-02.

2. The only issue which arose in this case is with respect to the taxability of Rs. 44,44,002 being excess amount of income over expenditure. The said surplus had arisen on account of advertisement contributions received from the holding company of the assessee-company which remained unexpended.

2.1 The broad facts with respect to the above case have been delineated in the connected appeal entitled *Yum! Restaurants (India) Pvt Ltd* v. *CIT*, being I. T. A. No. 192 of 2009, which was heard along with the present appeal. The judgment was reserved in both the appeals. (See *Yum! Restaurants (India) P. Ltd.* v. *CIT* [2010] 327 ITR 150 (Delhi)).

3. Briefly, the parent company, that is, Yum! Restaurants (India) Pvt. Ltd. (in short 'YRIPL') formerly known as Tricon Restaurants India Pvt. Ltd. was incorporated on March 17, 1994. YRIPL had a licence arrangement with Kentucky Fried Chicken International Holdings, Inc. (in short 'KFC') and Pizza Hut International LLC (in short 'PHILLC'). YRIPL sought permission from the Government of India, Ministry of Industry, Department of Industrial Policy and Promotion, Secretariat for Industrial Assistance (SIA), Foreign Collaboration, for setting up a wholly owned step-down subsidiary to manage retail restaurant business, for advertising and promotion at local store level, regional level and National level. By a letter

dated October 5, 1998, the SIA granted approval to YRIPL to set up a step-down wholly-owned subsidiary on the basis of a broad framework indicated by YRIPL. The broad framework being that the proposed new subsidiary company would be a non-profit enterprise which would be governed by the principle of mutuality. The wholly owned subsidiary, as indicated by YRIPL, was being set up to carry out and economise the cost of advertising and promotion by catering to the specific needs of its franchisees in order to enable them to concentrate on restaurant operations and management. The approval was granted on the condition that the subsidiary would be a non-profit enterprise and that it would not repatriate its dividends out of the country.

3.1 Upon receiving the requisite permission the assessee-company was incorporated on June 8, 1999.

3.2 In September, 2000, YRIPL, the assessee-company, as well as the franchisees entered into tripartite agreements. Under the agreement the assessee-company received contributions from the franchisees as well as the franchisees of YRIPL to the extent of 5 per cent. of the gross sales in order to carry on co-operative advertising. The agreement also envisaged that the purpose of incorporating the assessee-company was really to carry the marketing activities of each of the brands of which YRIPL was a licensee for the mutual benefit of the franchisees. The entire activity of the assessee-company was to be carried out on no-profit basis and that the assessee-company was obliged not to repatriate any dividends. The broad purpose of the agreement is best encapsulated in the following clauses :

> '2.2 TRIM will establish and operate brand funds in respect of each brand for the purpose of allocating and using the advertising contribution received from franchisee and other franchisee of Tricon operating restaurants under the brands. TRIM will allocate the advertising contribution received from the franchisees including franchisee for each restaurant to the respective brand funds established for that brand. It is agreed between the parties that the advertising contribution paid into a brand fund will be used for the AMP activities relating to that brand.
>
> 3.1 As and from the effective date, the franchisee will pay the advertising contribution of 5 per cent. of revenue for a particular month into the bank account of the brand fund established by TRIM by the tenth day of the following month. Details of the bank account of each brand fund set up by TRIM will be notified to franchisee by TRIM from time to time. Notwithstanding the aforesaid the executive committee of any brand (constituted under article 7 of this agreement)

may, by a three fourth majority, which shall be binding on all franchisees of Tricon including the franchisee, require the franchisee to pay the advertising contribution in advance. For the avoidance of doubt it is clarified and agreed that while recommending advance payment of advertising contribution the chairman will not have a casting vote.

Franchisee will spend an additional 1 per cent. of revenues, in the manner directed by Tricon and/or TRIM in writing from time to time, on such local store marketing, advertising, promotional and research expenditure proposed by franchisee and approved in advance by Tricon and/or TRIM during the relevant accounting period, in accordance with the requirements and guidelines set out in the manuals, provided that if franchisee fails to spend the full amount as directed by Tricon and/or TRIM franchisee will pay the unspent amount to TRIM within the period specified in a written demand from TRIM. Upon receipt of the unspent amount TRIM will spend the amount on regional and/or National advertising, promotions or research expenditure conducted by TRIM in its discretion . . .

*4.1 Tricon may at the request of TRIM, but subject to Tricon's sole and absolute discretion pay to TRIM any such amount(s) as it may deem appropriate to support the AMP activities during any accounting period. For the avoidance of doubt, it is clarified and agreed between the parties that Tricon shall have no obligation to pay any such amounts if it chooses not to do so . . .*

8.4 In the event there is any surplus left over in any of the brand funds at the end of an accounting period, TRIM shall be entitled to retain the surplus to be spent on AMP activities during the following accounting period. Alternatively, TRIM may, subject to the approval of its board of directors refund the surplus amounts to the franchisees including franchisee in the same proportion as the actual advertising contribution made by each franchisee including franchisee in that accounting period.

On the other hand, if there is a deficit in any of the brand funds at the end of an accounting period, the deficit will be carried forward to the next accounting period and be met out of the advertising contribution paid by the franchisees including franchisee for that accounting period. For the avoidance of doubt, it is agreed between the parties that Tricon and/or TRIM shall not be obliged to fund the deficit.

8.5 It is clearly understood and agreed between the parties that the only objective of TRIM is to co-ordinate the marketing activities of the brands including the mutual benefit of the franchisees including the franchisee. It is envisaged that no profits will be earned and no dividends will be declared by TRIM.'

3.3 It is in this background that on October 31, 2001 the assessee-company filed its return for the assessment year 2001-02. On August 27, 2002 the assessee's return was processed under section 143(1) of the Act. On October 24, 2002 the assessee's case was picked up for scrutiny and a notice under section 143(2) of the Act was issued to the assessee-company. During the course of scrutiny, queries were raised with the representatives of the assessee-company, whereupon it was revealed that the assessee-company had an excess income over expenditure amounting to Rs.44,44,002. However, the gross total income had been declared as 'nil'. The income and expenditure account as recorded in the order of the Assessing Officer read as follows :

| | *Rs.* |
|---|---|
| *'Income* | |
| Advertising contribution from franchises, holding company and key associates | 2,64,69,546 |
| *Expenditure* | |
| Advertising, marketing and promotional expenditure | 2,12,56,032 |
| Preliminary expenses | 4,54,992 |
| Administrative and other expenses | 1,90,272 |
| | 2,19,01,296 |
| Excess of expenditure carried forward from the previous year | (1,24,248) |
| Excess of income/(expenditure) over (expenditure)/income carried forward to the balance-sheet (included under current liabilities)' | 44,44,002 |

3.4 With the return the assessee-company had appended the notes broadly indicating that it was operating on the principles of mutuality and on 'no-profit' basis. The note further read that there was a complete identity between the contributors and the receipts of the fund, that is, the assessee-company. The assessee-company rendered services exclusively to the franchisees and that the franchisees had exclusive right over the surplus. The outlet of the franchisee did not derive any profit from the funds. The funds of the assessee-company could only be used for meeting expenses on their behalf or be returned to them.

4. The Assessing Officer examined the case law and the details submitted by the assessee-company. The Assessing Officer after examining the

contents of the SIA approval granted vide letter dated October 5, 1998 and the contents of the tripartite agreement returned the following finding of facts :

'It was seen from the details filed by the assessee-company that in terms with the SIA approval as per clause 3 as reproduced above in para VI.1, YRIPL and the franchisees will contribute fixed percentage of their revenues to the proposed new company, i. e., the assessee. Whereas clause 4.1 of the tripartite operating agreement as reproduced above in para VI.2, provides that YRIPL has no obligation to contribute any amount which is contradictory to the terms of approval of SIA.

Separate funds were to be maintained for KFC and Pizza Hut brands. Further as per clause 5.1 as reproduced above in para VI.2 of the operating agreement provides that bank account of each brand fund established by the assessee-company will be notifying to the franchisee and the franchisee will be paying the advertising contribution of 5 per cent. of revenues for a particular month into such bank account. However, it was seen brand funds was established by the assessee-company. In fact, YRIPL continued to receive the advertising contribution from the franchisee as was being done by it prior to setting up of the assessee-company. This findings show that the assessee-company has been used as a tool to evade tax on excess of income over expenditure incurred during the previous year. A chart giving complete details of contributions receivable by the assessee-company and amounts actually received by the assessee-company and YRIPL is being enclosed as annexure A. This annexure shows that most of the contribution has been received by YRIPL which is against the terms of SIA approval and even the clauses of Tripartite operating agreement.

VI.5 *Single Ledger Account—assessee-company and YRIPL—considered as one entity*

Information under section 133(6) was called from all the franchisees. The information received from such franchisees is analysed in the ensuing paras below. In their books of account, the franchisees have one ledger account for royalties, marketing, advertising payable to YRIPL/assessee-company. For them it is single entity. They have not maintained any separate account of assessee-company. A few instances are discussed below . . .

. . . The assessee-company was also informed about non-submission of details by Pepsi Foods Ltd. vide order sheet entry dated March

5, 2004. It is pertinent to mention here that as per details of contributions filed by the assessee-company M/s. Pepsi Food Ltd.'s marketing contributions of Rs. 32.70 lakhs was received by YRIPL.

All the above findings make it clear that the assessee-company was not operating in terms with the SIA approval.

*It was seen from the details of accrued marketing filed by the assessee-company during the course of assessment proceedings under section 143(2) of the Income-tax Act, 1961 in the case of M/s. Yum! Restaurants India Pvt. Ltd. pending before this office that not all the franchises are paying 5 per cent. of their revenues : e. g. M/s. Devyani International Private Limited and Speciality Restaurants were paying contribution at 4 per cent. instead of 5 per cent. as prescribed in the tripartite agreement. All the participants to the so-called brand fund or so-called 'mutual concern' should have been contributing equally or on equal proportion.*

It is further seen that as per clause 3 of SIA letter as reproduced in para VI.1 of this order the franchisees and YRIPL were required to make contribution or affix (a fixed percentage) of their respective revenue. However, as per clause 4.1 of the tripartite operating agreement as reproduced in para VI.2 of this order YRIPL is under no obligation to pay any contribution if it chooses not to do so which is totally in contradiction to SIA letter.'

4.1 From the aforesaid the Assessing Officer came to the conclusion that the assessee-company was not operating in terms of the SIA approval.

5. Based on these findings the Assessing Officer brought to tax a sum of Rs. 44,44,002 which was an excess of income over expenditure by rejecting the claim that it was a mutual concern.

6. Aggrieved by the same the assessee-company filed an appeal before the Commissioner of Income-tax (Appeals) (hereinafter referred to as the 'CIT(A)'). The Commissioner of Income-tax (Appeals), after analysing all the facts and the case law in issue, was of the view that all the participants in the module set up by the assessee-company were business concerns and the purpose of setting up of fund was a commercial purpose. The Commissioner of Income-tax (Appeals) observed that the advertising, marketing and promotional activities (hereinafter referred to as the 'APM activities') being a critical component of running a successful business venture, it is intrinsically linked to profit on sales of franchisees, that is, the contributors. It could not be said that the contributors' activity was immune from the taint of 'commerciality' and that unlike a club the assessee-company was not set up for social intercourse nor was it a set up for cultural

activity where the idea of profit or trade does not exist. What was essential was that there should not be any dealing with the outside body which results in benefit which promotes some commercial/business venture. He further held that though the form taken up to conduct its activity resembles a mutual concern, it could not however be denied that the contributions were made undoubtedly for business considerations. The Commissioner of Income-tax (Appeals) being of the view that the underlying purpose was solely for commercial consideration and excess of income over expenditure should be brought to tax.

7. Being aggrieved, the assessee-company preferred an appeal to the Tribunal. The Tribunal by the impugned judgment dismissed the appeal of the assessee-company after noting the facts of the case as well as the principle of mutuality invoked by the assessee-company to sustain its stand that the said excess of income over expenditure was not taxable. The Tribunal noted that in the present case the principles of mutuality was not applicable on account of the fact that apart from *contributions received from various franchisees contributions to the extent of Rs. 32.70 lakhs had also been received from Pepsi Foods Ltd. as also from YRIPL, who were neither franchisees nor beneficiaries*. As per the tripartite agreement it noted that contributions were received from YRIPL, that is, the parent company which was not under any obligation to pay. Therefore the essential requirements of a mutual concern were missing. This was especially so that since Pepsi Foods Ltd. and YRIPL who was a contributor to the fund did not benefit from the APM activities. Thus the Tribunal held that the principles of mutuality being not applicable to the excess of income over expenditure was required to be taxed.

8. Having heard the learned counsel Mr. C. S. Aggarwal, senior advocate for the assessee-company and Ms. Prem Lata Bansal for the Revenue we are of the view that the judgment deserves to be sustained. The principle of mutuality as enunciated by the courts in various cases is applicable to a situation where the income of the mutual concern is the contributions received from its contributors. The expenses incurred by the mutual concern are incurred from such contributions and hence on the principle that no man can do business with himself, the excess of income over expenditure is not amenable to tax. However, in the present case, the authorities below have returned a finding of fact that the fund has contributors such as Pepsi Foods Ltd. which do not benefit from the APM activities. Moreover, the principle of mutuality is applicable to those entities whose activities are not tinged with commercial purpose. As a matter of fact in the instant case, the parent company, i. e., YRIPL, which has also contributed to the brand

fund is under the agreement under no obligation to do so. The contributions of YRIPL are at its own discretion. Thus, looking at the facts obtaining in the present case, it is quite clear that the principle of mutuality would not be applicable to the instant case. This was the only stand taken by the appellant before the authorities below. In these circumstances we are of the opinion that the impugned judgment of the Tribunal does not call for interference. The authorities below have returned pure findings of fact which are not perverse to our minds. No substantial question of law arises for our consideration. Resultantly, the appeal is dismissed."

*Balbir Singh*, Senior Advocate, (*Ms. Anuradha Dutt*, *Ms. Fereshte D. Sethna*, *Tushar Jarwal*, *Rahul Sateeja*, *Ms. B. Vijayalakshmi Menon*, and *Deepak Thakur*, Advocates, with him) for the appellant.

*V. Shekhar*, Senior Advocate, (*Ms. Praveen Gautam*, *Shashank Shekhar* and *Ms. Sheetal Rajput*, Advocates, with him) for the respondent.

**JUDGMENT**

The judgment of the court was delivered by

1 A. M. KHANWILKAR J.—The moot question involved in the present appeal bears upon the applicability of the doctrine of mutuality qua the assessee-company, a fully owned subsidiary of Yum! Restaurants (India) Pvt. Ltd. (for short, "YRIPL"), formerly known as Tricon Restaurants India Pvt. Ltd., incorporated for undertaking the activities relating to advertising, marketing and promotion (for short, "AMP activities") for and on behalf of YRIPL and its franchisees.

2 This appeal assails the final judgment and order dated April 1, 2009 passed by the High Court of Delhi at New Delhi (for short, "the High Court") in I. T. A. No. 1433 of 2008 wherein the question of taxability of Rs. 44,44,002 (rupees forty four lakhs forty four thousand two only), being the excess of income over expenditure for the assessment year 2001-02, was settled in favour of the Revenue and against the assessee, thereby confirming the orders of the Income-tax Appellate Tribunal (for short, "the Tribunal"), Commissioner of Income-tax (Appeals) (for short, the "CIT(A)") and the Assessing Officer. The preceding forums, without any exception, have returned consistent verdicts refusing to acknowledge the assessee-company as a mutual concern and denying any exemption from taxability.

3 The appellant-company Yum! Restaurants (Marketing) Private Limited (for short, "YRMPL" or "assessee-company" or "assessee") was incorporated by YRIPL as its fully owned subsidiary after having obtained approval from the Secretariat for Industrial Assistance (for short "SIA") for the

purpose of economisation of the cost of advertising and promotion of the franchisees as per their needs. The approval was granted subject to certain conditions as regards the functioning of the assessee, whereby it was obligated to operate on a non-profit basis on the principles of mutuality. The relevant clauses of the approval granted by the SIA for the aforementioned operations read thus :

"3. It is noted that the broad framework within which such subsidiary shall be managed and operated in India is as follows :

The franchises and Tricon India will both make contribution of a fixed percentage of their respective revenues (net of taxes) to the proposed new company on regular basis ;

The proposed new company would be a non-profit enterprise governed by the principles of mutuality. No part of the contributions or other income shall enure to the benefit of any individual contributor ;

The contributors will be optimally used by the proposed new company to economise the cost of advertising and promotion to cater to the specific needs of franchisees to concentrate on restaurant operations and management ;

The management of the proposed new company shall vest with Tricon India and application of contributions will be decided by Tricon India in consultation with the franchisee ; . . .

The approval is subject to the condition that the step down subsidiary would be a non-profit enterprise and would not be allowed to repatriate dividends."

In furtherance of the approval, the assessee entered into a tripartite **4** operating agreement (for short, the "tripartite agreement") with YRIPL and its franchisees, wherein the assessee-company received fixed contributions to the extent of 5 per cent. of gross sales for the proper conduct of the advertising, marketing and promotional activities for the mutual benefit of the parent company and the franchisees. The terms of the tripartite agreement, to the extent relevant for the consideration of the present case, are produced thus :

"2.2 TRIM will establish and operate brand funds in respect of each brand for the purpose of allocating and using the advertising contribution received from the franchisee and other franchisee of Tricon operating restaurants under the brands. TRIM will allocate the advertising contribution received from the franchisees including franchisee for each restaurant to the respective brand funds established for that

brand. It is agreed between the parties that the advertising contribution paid into a brand fund will be used for the AMP activities relating to that brand.

3. *Franchisee advertising contributions*

3.1 As and from the effect date, franchisee will pay the advertising contribution of 5 per cent. of revenues for a particular month into the bank account of the brand fund established by TRIM by the 10th day of the following month. Details of the bank account, of each brand fund set up by TRIM will be notified to franchisee by TRIM from time to time. Notwithstanding the aforesaid, the executive committee of any brand (constituted under article 7 of this agreement) may, by a three fourth majority, which shall be binding on all franchisees of Tricon including the franchisee, require the franchisee to pay the advertising contribution in advance. For the avoidance of doubt it is clarified and agreed that while recommending advance payment of advertising contribution the chairman will not have a casting vote.

Franchise will spend an additional 1 per cent. of revenues, in the manner directed by Tricon and/or TRIM in writing from time to time, on such local store marketing, advertising, promotional and research expenditure proposed by franchisee and approved in advance by Tricon and/or TRIM during the relevant accounting period, in accordance with the requirements and guidelines set out in the manuals, provided that if franchisee fails to spend the full amount as directed by Tricon and/or TRIM franchisee will pay the unspent amount to TRIM within the period specified in a written demand from TRIM. Upon receipt of the unspent amount TRIM will spend the amount on regional and/or National advertising, promotions or research expenditure conducted by TRIM in its discretion . . .

4.1 *Tricon may at the request of TRIM, but subject to Tricon's sole and absolute discretion pay to TRIM any such amount(s) as it may deem appropriate to support the AMP [sic] activities during any accounting period for the avoidance of doubt, it is clarified and agreed between the parties that Tricon shall have no obligation to pay any such amounts if it chooses not to do so . . .*

8.4 In the event there is any surplus left over in any of the brand funds at the end of an accounting period, TRIM shall be entitled to retain the surplus to be spent on AMP activities during the following accounting period. Alternatively, TRIM may, subject to the approval of its board of directors refund the surplus amounts to the franchisees including franchisee in the same proportion as the actual advertising

contribution made by each franchisee including franchisee in that accounting period.

On the other hand, if there is a deficit in any of the brand funds at the end of an accounting period, the deficit will be carried forward to the next accounting period and be met out of the advertising contribution paid by the franchisees including franchisee for that accounting period. For the avoidance of doubt, it is agreed between the parties that Tricon and/or TRIM shall not be obliged to fund the deficit.

8.5 It is clearly understood and agreed between the parties that the only objective of TRIM is to co-ordinate the marketing activities of the brands including the mutual benefit of the franchisees including the franchisee. It is envisaged that no profits will be earned and no dividends will be declared by TRIM." (emphasis[1] supplied)

5 For the assessment year under consideration, the assessee filed its returns stating the income to be "nil" under the pretext of the mutual character of the company. The same was not accepted by the Assessing Officer, who observed thus :

"VI.7.3 As per the SIA letter dated October 5, 1998, the assessee-company along with the franchisees were to contribute a fix percentage of its revenue to YRMPL. However as per clause 4.1 of tripartite operating agreement submitted by YRMPL, the assessee-company had its sole absolute discretion to pay to YRMPL any amount as it may deem appropriate and that YRIPL shall have no obligation to pay any such amounts if it chooses not to do so. This clearly shows that YRIPL was under no legal obligation to pay any amount of contribution as per its own version reflected from tripartite agreement."

6 The imposition of liability by the Assessing Officer was upheld by the Commissioner of Income-tax (Appeals) on the ground of taint of commerciality in the activities undertaken by the assessee-company, wherein it was observed thus :

"1.14 . . . The AMP activity is quite a critical component of running a successful business venture, it is intrinsically linked to sales and profit of the franchisees, the contributors. Accordingly it cannot be said that such activity is immune from the taint of commerciality. Unlike in the cases of a club, the appellant-company is not existing for any social inter course nor is it for cultural activities where the idea of profit or trade does not exist. What is essential is that there should

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not be any dealing with outside body which results in a benefit which promotes some commercial/business venture. There should not be any profit earning motive in any transaction directly or indirectly. In fact in the appellant's case the essence of mutuality also appears to be missing in that there is no instance or scope of say trading between persons associating together. Thus though the form taken up to conduct its revenue activity undoubtedly resemble a mutual concern but the contributions made on the other hand are undeniably for business considerations. In my opinion, taking an overall view of the intent and motive of the appellant-company to form a 'mutual concern' it can be concluded that the underlying purpose was solely for commercial consideration. Therefore in view of the above as demonstrated by the appellant-company the excess of receipts over the expenditure, i.e., the surplus in my opinion would be income liable to tax . . ."

7 The liability was further confirmed by the Tribunal, wherein the essential ingredients of the doctrine of mutuality were found to be missing. It observed thus :

"11 . . . Firstly the Government order sanctioning setting up of the wholly owned subsidiary prescribes that the approval is subject to the condition that such subsidiary would be a non-profit enterprise and is also not entitled to repatriate dividends. The main object of the assessee-company reveals that it is to carry out advertising, marketing and promotion for brands owned by its parent company. The main plank of the assessee's arguments is that the principles of mutuality will apply and hence the income cannot be taxed. Time and again various courts have held that where there is complete identity between the contributors and the participators or the beneficiaries, only then such principles can be applied. *However, in the present case it is seen that apart from contributions is also received from M/s. Pepsi Foods Ltd. and YRIPL. Pepsi Foods Ltd. is neither a franchisee nor a beneficiary. Similarly some contribution is also received from YRIPL which YRIPL is not under any obligation to pay. Thus it can be said that essential requirement that of the contributors to the common fund are either to participate in the surplus or they are beneficiaries of the contribution is missing. Through the common AMP activities no benefit accrues to Pepsi Foods Ltd. or YRIPL. Accordingly the principles of mutuality cannot be applied.* It is a different fact that the assessee was established with the object not to make profit but it is also a fact that there is a surplus in the hands of the assessee which arose due to

contribution from certain persons who were neither the beneficiaries nor have right to receive the surplus . . .” (emphasis[1] supplied)

**8** The consistent line of opinion recorded by the aforementioned three forums was further approved in appeal by the High Court vide impugned judgment, by observing thus :

“8. . . . The principle of mutuality as enunciated by the courts in various cases is applicable to a situation where the income of the mutual concern is the contributions received from its contributors. The expenses incurred by the mutual concerns are incurred from such contributions and hence on the principle that no man can do business with himself, the excess of income over expenditure is not amenable to tax. However, in the present case the authorities below have returned a finding of fact that the fund has contributors such as Pepsi Foods Ltd. which do not benefit from the APM activities. Moreover, the principle of mutuality is applicable to those entities whose activities are not tinged with commercial purpose. As a matter of fact in the instant case the parent company, i.e., YRIPL which has also contributed to the brand fund is under the agreement under no obligation to do so. The contributions of YRIPL are at its own discretion. Thus, looking at the facts obtaining in the present case, it is quite clear that the principle of mutuality would not be applicable to the instant case . . . ”

**9** On cogitating over the rival submissions, we reckon that the following questions of law would arise for our consideration in the present case :

“(i) Whether the assessee-company would qualify as a mutual concern in the eyes of law, thereby exempting subject transactions from tax liability ?

(ii) Whether the excess of income over expenditure in the hands of the assessee-company is not taxable ?”

**10** The appellant-assessee has contended that the sole objective of the assessee-company was to carry on the earmarked activities on a no-profit basis and to operate strictly for the benefit of the contributors to the mutual concern. It has further been contended that the assessee-company levies no charge on the franchisees for carrying out the operations. While assailing the observations made in the impugned judgment, holding that Pepsi Foods Ltd. and YRIPL are not beneficiaries of the concern, the assessee-company has urged that YRIPL is the parent company of the assessee and earns fixed percentage from the franchisees by way of royalty. Therefore, it

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benefits directly from enhanced sales as increased sales would translate into increased royalties. A similar argument has been advanced as regards Pepsi Foods Ltd. It is stated that under a marketing agreement, the franchisees are bound to serve Pepsi drinks at their outlets and thus, an increase in the sales at KFC and Pizza Hut outlets as a result of AMP activities would lead to a corresponding increase in the sales of Pepsi. To add weight to this argument, it has been brought to our notice that Pepsi was also advertised by the franchisees in their advertising and promotional material, along with Pizza Hut and KFC, and a copy of the said material has been placed on record.

**11** As regards the doctrine of mutuality, it is urged by the assessee-company that the doctrine merely requires an identity between the contributors and beneficiaries and it does not contemplate that each member should contribute to the common fund or that the benefits must be derived by the beneficiaries in the same manner or to the same extent. Reliance has been placed by the appellant upon reported decisions to draw a parallel between the functioning of the assessee-company and clubs to support the presence of mutuality.

**12** The Revenue-respondent has countered the submissions made by the assessee-company by submitting that the moment a non-member joins the common pool of funds created for the benefit of the contributors, the taint of commerciality begins and mutuality ceases to exist in the eyes of law. It has been submitted that the assessee-company operated in contravention of the SIA approval as contributions were received from Pepsi, despite it not being a member of the brand fund. To buttress this submission, it is urged that once the basic purpose of benefiting the actual contributors is lost, mutuality stands wiped out.

**13** We have heard Mr. Balbir Singh, learned senior counsel for the appellant and Mr. V. Shekhar, learned senior counsel for the respondent.

*Re : Question (i)*

**14** The doctrine of mutuality traces its origin from the basic principle that a man cannot engage into a business with himself. For that reason, it is deemed in law that if the identity of the seller and the buyer ; or the vendor and the consumer ; or the contributor and the participator is marked by oneness, then a profit motive cannot be attached to such a venture. Thus, for the lack of a profit motive, the excess of income over the expenditure or the "surplus" remaining in the hands of such a venture cannot be regarded as "income" taxable under the Income-tax Act, 1961 (for short, "the 1961 Act"). What is taxable under the 1961 Act is "income" or "profits" or "gains" as they accrue to a person in his dealings with other party or

parties that do not share the same identity with the assessee. For income, there is an underlying exchange of a commercial nature between two different entities. In *CIT* v. *Bankipur Club Ltd.*[1], this court observed on the nature of liability under the 1961 Act thus[2] :

> "6. Under the Income-tax Act (hereinafter referred to as 'the Act') what is taxed is, the 'income, profits or gains earned or 'arising', 'accruing' to a person'. The question is whether in the case of members' clubs - a species of mutual undertaking - in rendering various services to its members which result in a surplus, the club can be said to 'have earned income or profits'. In order to answer the question, it is necessary to have a background of the law relating to 'mutual trading' or 'mutual undertaking' and a 'members club'."

The law regarding the tenets of mutuality is no more res integra. It has **15**
been settled in a catena of judicial pronouncements and academic works across multiple jurisdictions. In *Bangalore Club* v. *CIT*[3], this court authoritatively quoted one of the earliest judicial pronouncements in *New York Life Insurance Co.* v. *Styles (Surveyor of Taxes)* [1889] 2 TC 460 thus[4] :

> "When a number of individuals agree to contribute funds for a common purpose . . . and stipulate that their contributions, so far as not required for that purpose, shall be repaid to them. I cannot conceive why they should be regarded as traders, or why contributions returned to them should be regarded as profits."

The proposition of law is restated in *Bankipur Club* (supra) and *Bangalore Club* (supra) by placing reliance upon the following extract from *Simon's Taxes*, Volume B, 3rd Edition, pages 159, 167 :

> ". . . it is settled law that if the persons carrying on a trade do so in such a way that they and the customers are the same persons, no profits or gains are yielded by the trade for tax purposes and therefore no assessment in respect of the trade can be made. Any surplus resulting from this form of trading represents only the extent to which the contributions of the participators have proved to be in excess of requirements. Such a surplus is regarded as their own money and returnable to them. In order that this exempting element of mutuality should exist it is essential that the profits should be capable of coming back at some time and in some form to the persons to whom the goods were sold or the services rendered . . . "

1. [1997] 226 ITR 97 (SC) ; 1997] 5 SCC 394.
2. Page 101 of 226 ITR.
3. [2013] 350 ITR 509 (SC) ; [2013] 5 SCC 509.
4. Page 517 of 350 ITR.

**16** In order to undertake the examination of mutuality, we gainfully advert to *English and Scottish Joint Co-operative Wholesale Society Ltd.* v. *Commr. of Agrl. I. T.*[1], which has been quoted with approval by this court in *CIT* v. *Royal Western India Turf Club Ltd.*[2] and *Bangalore Club* (supra). The aforestated stream of judicial pronouncements expound three conditions/tests to prove the existence of mutuality[3] :

> "(i) Identity of the contributors to the fund and the recipients from the fund ;
>
> (ii) Treatment of the company, though incorporated as a mere entity for the convenience of the members and policy holders, in other words, as an instrument obedient to their mandate ; and
>
> (iii) Impossibility that contributors should derive profits from contributions made by themselves to a fund which could only be expended or returned to themselves."

Whereas the legal position on what amounts to a mutual concern stands fairly settled, the factual determination of the same on a case to case basis poses a complex issue that requires deeper examination. Such examination ought to be conducted in the light of the tests enunciated above.

*Common identity*

**17** The first element involves the test of commonality of identity between the members or participators in the mutual concern and the beneficiaries thereof. Succinctly put, this limb of the three-pronged test requires that no person ought to contribute to the common fund without having the entitlement to participate as a beneficiary in the surplus thereof. Conversely, no person ought to participate as a beneficiary without first having been a contributor or a member of the class of contributors to the common fund. Common identity, as it occurs in the present context, signifies that the class of members should stay intact as the transaction progresses from the stage of contributions to that of returns/surplus. It must manifest uniformity in the class of participants in the transaction. The moment such a transaction opens itself to non-members, either in the contribution or the surplus, the uniformity of identity is impaired and the transaction assumes the taint of a commercial transaction. The emphasis on the words member and non-member is of import because the doctrine of mutuality does not prohibit the inclusion or exclusion of new members. What is prohibited is the infusion of a participant in the transaction who does not become a "member" of the common fund, at par with other members, and yet participates

1. [1948] 16 ITR 270 (PC) ; AIR 1948 PC 142
2. [1953] 24 ITR 551 (SC) ; AIR 1954 SC 85.
3. Page 279 of 16 ITR.

either in the contribution or surplus without subjecting itself to mutual rights and obligations. The principle of common identity prohibits any one-dimensional alteration in the nature of participation in the mutual fund as the transaction fructifies. Any such alteration would lead to the non-uniform participation of an external element or entity in the transaction, thereby opening the scope for a manifest or latent profit-based dealing in the transaction with parties outside the closed circuit of members. It would be amenable to income-tax as per section 2(24) of the 1961 Act.

*Completeness of identity*

Coterminous with the requirement of common identity, as discussed above, the law also contemplates a completeness of identity between the contributors and participators. The theory of completeness of identity presupposes the contributors and participators to be two separate classes, but there is oneness or equality in the matter of sharing of surplus/profits. This is to ensure that there is no interference of any alien commercial entity in the transaction. With the interference of any alien entity, the idea of conducting business with oneself is defeated and any profits or gains accruing therefrom become subject to tax liability. This proposition of law is succinctly predicated in *British Tax Encyclopaedia*[1], which reads thus : **18**

> ". . . For this doctrine to apply it is essential that all the contributors to the common fund are entitled to participate in the surplus and that all the participators in the surplus are contributors, so that there is complete identity between contributors and participators. This means identity as a class, so that at any given moment of time the persons who are contributing are identical with the persons entitled to participate ; it does not matter that the class may be diminished by persons going out of the scheme or increased by others coming in."

It is pertinent to note that in order to determine the breach in mutuality, the court is well within its powers to go beyond the periphery of the concern and undertake an examination akin to the lifting of the veil in order to discern the real nature thereof.

In the present case, it is indisputable that Pepsi Foods Ltd. is a contributor to the common pool of funds. However, it does not participate in the surplus as a beneficiary for at least two reasons – first, Pepsi is not a member of the purported mutual concern as the tripartite agreement as well as the terms of SIA approval permit only "franchisees" to become members of the mutual concern. Notably, Pepsi Foods Ltd. is not a franchisee and thus, it cannot participate in the surplus. Second, Pepsi does not **19**

1. *British Tax Encyclopaedia* (I), 1962 Edition, pages 1200 and 1201.

enjoy any right of participation in the surplus or any right to receive back the surplus which are mandatory ingredients to sustain the principle of mutuality.

**20** We find it noteworthy that the tripartite agreement requires the assessee-company to constitute a separate brand fund for each franchisee as stated in clause 2.2 of the said agreement, which reads thus :

> "2.2 TRIM will establish and operate brand funds *in respect of each Brand*, for the purpose of allocating and using the advertising contribution received from franchisee and other franchisee of Tricon operating restaurants under the brands TRIM will allocate the advertising contribution received from the franchisees including franchisee for each restaurant to the parties that the advertising contribution paid into a brand fund will be used for the AMP activities relating to that brand." (emphasis[1] supplied)

Since no brand fund, as contemplated above, has been constituted for Pepsi Foods Ltd., it does not become a part of the purported tripartite mutual arrangement so as to qualify as a beneficiary of the mutual operations. The definition clause of the tripartite agreement adds weight to this finding. "Advertising contribution", as defined in the definition clause means :

> "the advertising contributions which franchisee has agreed to pay to Tricon pursuant to [sic] the franchisee agreements."

Furthermore, "franchise agreements", as defined in the definition clause, means agreements executed between Tricon and franchisee. As a corollary, what follows is that for any amount received by the assessee-company to be treated as an advertising contribution, it must be paid by a franchisee, that too in the aftermath of a prior franchisee agreement to that effect. In the light of the prevailing relationship, there is no such franchisee agreement between Tricon or TRIM and Pepsi Foods Ltd. and therefore, the amounts received from Pepsi Foods Ltd. cannot be viewed as advertising contributions "from a member of the mutual undertaking" as such.

**21** In the present case, therefore, the assessee-company is realising money both from the members as well as non-members in the course of the same activity carried on by it. This court, in *Royal Western India Turf Club Ltd.* (supra) has categorically held such operations to be antithetical to mutuality. We deem it apposite to take note of the dictum in *Bankipur Club* (supra), wherein this principle has been restated thus[2] :

1. Here printed in italics.
2. Page 110 of 226 ITR.

> ". . . if the object of the assessee-company claiming to be a 'mutual concern' or 'club', is to carry on a particular business and the money is realised both from the members and from non-members, for the same consideration by giving the same or similar facilities to all alike in respect of the one and the same business carried on by it, the dealings as a whole disclose the same profit-earning motive and are alike tainted with commerciality . . . and the resultant surplus is profit-income liable to tax."

**22** The contention of the assessee-company that Pepsi Foods Ltd., in fact, does benefit from the mutual operations by virtue of its exclusive contracts with the franchisees is tenuous, as the very basis of mutuality is missing as far as Pepsi Foods Ltd. is concerned, as discussed hitherto. Even if any remote or indirect benefit is being reaped by Pepsi Foods Ltd., the same cannot be said to be in lieu of it being a member of the purported mutual concern and therefore, cannot be used to fill the missing links in the chain of mutuality. Concededly, the surplus of a mutual operation is meant to be utilised by the members of the mutual concern as members enjoy a proximate connection with the mutual operation. Non-members, including Pepsi Foods Ltd., stand on a different footing and have no proximate connection with the affairs of the mutual concern. The exclusive contract between the franchisees and Pepsi Foods Ltd. stands on an independent footing and YRIPL as well as the assessee-company are not responsible for implementation of this contract. Resultantly, the first limb of the three-pronged test stands severed.

*Non-profiteering and obedience to mandate*

**23** Whereas the doctrine of mutuality stands debunked with the failure of the first test, let us, none the less, examine the other two tests in the present factual scenario. Indubitably, the receipt of money from an outside entity without affording it the right to have a share in the surplus does not only subjugate the first test of common identity, but also contravenes the other two conditions for the existence of mutuality, i.e., impossibility of profits and obedience to the mandate. The mandate of the assessee-company was laid down in the SIA approval wherein the twin conditions of mutuality and non-profiteering were envisioned as the sine qua non for the functioning of the assessee-company. The contributions made by Pepsi Foods Ltd. tainted the operations of the assessee-company with commerciality and concomitantly contravened the prerequisites of mutuality and non-profiteering.

**24** The mutuality and non-profiteering character of a concern are to be determined in the light of its actual working structure and the factum of

corporation or incorporation or the form in which it is clothed is immaterial. It is, therefore, imperative to examine the actual functional framework of the assessee-company in the light of the status of YRIPL (parent company) vis-a-vis other members/franchisees. As per the terms of the SIA approval, YRIPL and franchisees were equally obligated to make contribution of a fixed percentage to the assessee-company. This requirement was incorporated as a precondition for the grant of permission to operate as a mutual concern. Clause 3 of the approval letter reads thus :

> "The franchises and Tricon Indian will both make contribution of a fixed percentage of their respective revenues (net of taxes) to the proposed new company on regular basis :"

However, drifting from this mandate, the tripartite agreement made it discretionary upon YRIPL to contribute to the common pool, thereby putting it at a higher pedestal than the franchisees. Clause 4.1 of the tripartite agreement reads thus :

> "4.1 Tricon may at the request of TRIM, *but subject to Tricon sole and absolute discretion pay to TRIM any such amount(s)* as it may deem appropriate to support the AMP activities during the accounting period for the avoidance of doubt, it is clarified and agreed between the parties that *Tricon shall have no obligation to pay any such amounts if it chooses not to do so*." (emphasis[1] supplied)

Thus, clause 4.1 is not in conformity with the terms of approval. Furthermore, it is noteworthy that the management of the assessee-company was under full and absolute control of its parent company YRIPL. Be it also noted that the participation of the franchisees in the management of the assessee-company was again subject to approval by YRIPL, which falls within its sole discretion. Clause 7.1 of the tripartite agreement reads thus :

> "7.1 The management and operations of TRIM will be carried out by its board of directors in accordance with the articles of association of TRIM, the terms of which shall be read as a part of this agreement. The board of directors of TRIM will be nominated by Tricon from time to time in accordance with the articles of association of TRIM. The board of directors of TRIM shall consist of a minimum number of five directors. *Out of the five directors Tricon may, in its absolute and sole discretion, nominate one representative each of two franchisees (to be selected by Tricon on a rational basis) to be appointed as directors on the board of directors of TRIM.* Such nominees to hold office for a period of one year from the date of their appointment, in the event

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the representative of the franchisee is nominated to the board of directors of TRIM. Franchisee agrees and undertakes to cause such representative to (i) accept such appointment as and when the same is made ; and (ii) to resign from the post of director on the expiry of one year from the date of appointment or earlier, if so requested by Tricon." (emphasis[1] supplied)

**25** The net effect of the aforequoted clauses is to render the preconditions for the grant of approval, as otiose. It also becomes amply clear that YRIPL and the franchisees stand on two substantially different footings. For, the franchisees are obligated to contribute a fixed percentage for the conduct of AMP activities whereas YRIPL is under no such obligation in utter violation of the terms of SIA approval. Moreover, even upon request for the grant of funds by the assessee-company, YRIPL is not bound to accede to the request and enjoys a "sole and absolute" discretion to decide against such request. That members of a financial concern exercise mutual control over its management without the scope of prejudicial exercise of power by one class of members over the others is the quintessence for the existence of a mutual concern. The word "mutual" offers guidance to this effect. Literally understood, the word "mutual" points towards reciprocity and a mutual arrangement is one in which the members/parties have reciprocal rights or understanding or arrangement. An arrangement wherein one member is subjected to the absolute discretion of another, in such a manner that the entire liability may fall upon one whereas benefits are reaped by all, is antithesis to the mutual character in the eyes of law.

**26** The contention advanced by the appellant that it is not mandatory for every member of the mutual concern to contribute to the common pool fails to advance the case of the appellant. It is no doubt true that every member of the mutual concern might not be required to contribute to the common pool at all times. However, it does not mean that one member cannot be made to contribute under any pretext whatsoever. For, that would amount to the grant of an overriding position to a member in the mutual agreement, extending up to even overruling the requests for contribution from other members for mutual necessity. It is this all-pervasive overriding position of one member over the others that negates the effect of mutuality. There is a fine line of distinction between absence of obligation and presence of overriding discretion. In the present case, YRIPL enjoys the latter at the detriment of the franchisees of the purported undertaking, both in matters of contribution and management. In a mutual concern, it is no doubt true that an obligation to pay may or may not be there,

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but in the same breath, it is equally true that an overriding discretion of one member over others cannot be sustained, in order to preserve the real essence of mutuality wherein members contribute for the mutual benefit of all and not of one at the cost of others.

**27** More importantly, an examination of the judicial decisions relied upon by the parties brings out the settled legal position that in order to qualify as a mutual concern, the contributors to the common fund either acquire a right to participate in the surplus or an entitlement to get back the remaining proportion of their respective contributions. In the present scheme of things, clause 8.4 provides that :

> "8.4 In the event there is any surplus left over in any of the brand funds at the end of an accounting period, TRIM shall be entitled to retain the surplus to be spent on AMP activities during the following accounting period. *Alternatively, TRIM may, subject to the approval of its board of directors, refund the surplus amounts to the franchisees* including franchisee in the same proportion as the actual advertising contribution made by each franchisee including franchisee in that accounting period." (emphasis[1] supplied)

**28** Contrary to the abovestated legal position, clause 8.4 makes it clear that the franchisees do not enjoy any "entitlement" or "right" on the surplus remaining after the operations have been carried out for a given assessment year. The clause provides that the assessee-company may refund the surplus subject to the approval of its board of directors. It implies that the franchisees/contributors cannot claim a refund of their remaining amount as a matter of right. Be it noted that the raison d'etre behind the refund of surplus to the contributors or mandatory utilisation of the same in the subsequent assessment year is to reduce their burden of contribution in the next year proportionate to the surplus remaining from the previous year. Thus, the fulfilment of this condition becomes essential. In the present case, even if any surplus is remaining in a given assessment year, it is unlikely to reduce the liability of the franchisees in the following year as their liability to the extent of 5 per cent is fixed and non-negotiable, irrespective of whether any funds are surplus in the previous year. The only entity that could derive any benefit from the surplus funds is YRIPL, i.e. the parent company. This is antithetical to the third test of mutuality.

**29** Be that as it may, the dispensation predicated in the tripartite agreement may entail in a situation where YRIPL would not contribute even a single penny to the common pool and yet be able to derive profits in the form of royalties out of the purported mutual operations, created from the fixed 5

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per cent. contribution made by the franchisees. This would be nothing short of derivation of gains/profits out of inputs supplied by others. That cannot be countenanced as being violative of the basic essence of mutuality. The doctrine of mutuality, in principle, entails that there should not be any profit earning motive, either directly or indirectly. The third test of mutuality, quoted above, requires that the purported mutual operations must be marked by an impossibility of profits and this crucial test is also not fulfilled in the present case.

30 Furthermore, the exemption granted to a mutual concern is premised on the assumption that the concern is being run for the mutual benefit of the contributors and the contributions made by the members ought to be directed in that direction. Contrary to this fundamental tenet, clause 8.1 of the tripartite agreement relieves the assessee-company from any specific obligation of spending the amounts received by way of contributions for the benefit of the contributors. It explicates that the assessee-company does not hold such amount under any implied trust for the franchisees, and reads thus :

> "8.1 . . . Notwithstanding the foregoing, any amount paid by franchisee to TRIM will not be required to be spent for the specific benefit, either direct or indirect, of franchisee or the business and no express or implied trust will be created in respect of such amount. Additionally, franchisee will not have any claim or action against Tricon and/or TRIM in connection with the level of success of any such advertising, marketing, promotion, research or test."

31 A priori, it must follow that the assessee-company had acted in contravention of the terms of approval. Notably, the SIA approval or Government approval was not only a binding document but also a conditional document with a defined set of preconditions for the functioning of the assessee-company as a mutual concern. The SIA approval categorically reads that the grant of approval is subject to the terms and conditions specified therein and any contravention thereof would be infraction of the mandate of the Government approval.

32 The appellant had urged that no fixed percentage of contribution could be imputed upon YRIPL as it does not operate any restaurant directly and thus, the actual volume of sales cannot be determined. At the very outset, this argument holds no water as YRIPL receives fixed percentage of royalty from the franchisees on the sales. We say so because if the franchisees could be obligated with a fixed percentage of contribution, 5 per cent. in the present case, it is unfathomable as to why the same obligation ought not to apply to YRIPL.

**33** Be it noted that the text of the tripartite agreement points towards the true intent of the formation of the assessee-company as a step down subsidiary. For, clause C predicates thus :

> "C. TRIM has been established as a wholly owned step down subsidiary of Tricon to manage of the retail restaurant business, the advertising medial and promotion at regional level and national level of KFC, Pizza Hut and other brands currently owned or acquired in future by Tricon and on its parents and of its associate company."

In the absence of any ambiguity, the terms of a contract are to be understood in their ordinary and natural sense, thus revealing the true intent of the contracting parties. The aforequoted clause clearly points towards the fact that the assessee-company was formed to manage business on behalf of the holding company. In its true form, it was not contemplated as a non-business concern because operations integral to the functioning of a business were entrusted to it.

**34** The doctrine of mutuality bestows a special status to qualify for exemption from tax liability. It is a settled proposition of law that exemptions are to be put to strict interpretation. The appellant having failed to fulfil the stipulations and to prove the existence of mutuality, the question of extending exemption from tax liability to the appellant, that too at the cost of public exchequer, does not arise. Taking any other view would entail in stretching the limits of construction. In *The Law of Taxation by Thomas M. Cooley*[1], the rule regarding strict construction of exemptions is succinctly summarised thus :

> "672. *Strict construction.*—Rule stated. An intention on the part of the Legislature to grant an exemption from the taxing power of the State will never be implied from language which will admit of any other reasonable construction. Such an intention must be expressed in clear and unmistakable terms, or must appear by necessary implication from the language used, for it is a well-settled principle that, when a special privilege or exemption is claimed under a statute, charter or act of incorporation, it is to be construed strictly against the property owner and in favour of the public. This principle applies with peculiar force to a claim of exemption from taxation. Exemptions are never presumed, the burden is on a claimant to establish clearly his right to exemption, and an alleged grant of exemption will be strictly construed and cannot be made out by inference or implication but must be beyond reasonable doubt . . . Moreover, if an exemption is found to exist, it must not be enlarged by construction, since the

1. *Thomas M. Cooley, The Law of Taxation*, 4th Edition, Volume 2, page 671.

reasonable presumption is that the State has granted in express terms all it intended to grant at all, and that unless the privilege is limited to the very terms of the statute the favour would be extended beyond what was meant . . . "

35 The assessee-company has relied upon reported decisions to establish a parallel between the operations carried out by itself and clubs. Upon closer scrutiny, however, we find that the authorities cited by the appellant do not advance its case because of the structural differences between the operations carried out by the purported mutual concern (assessee-company) and clubs. In the case of clubs, the operations are exempted from taxability because of the underlying notion that they operate for the common benefit of the members wishing to enter into a social exchange with no commercial intent. Further, all the members of the club not only have a common identity in the concern but also stand on an equal footing in terms of their rights and liabilities towards the club or the mutual undertaking. Such clubs are a means of social intercourse, as rightly observed by Commissioner of Income-tax (Appeals) in the present case, and are not formed for the facilitation of any commercial activity. On the contrary, the purported mutual concern in the present case undertakes a commercial venture wherein contributions are accepted both from the members as well as non-members, as discussed earlier. Moreover, one member is vested with a myriad set of powers to control the functioning and interests of other members (franchisees), even to their detriment. Such an assimilation cannot be termed as a case of ordinary social intercourse devoid of commerciality.

*Re : Question (ii)*

36 Once it is conclusively determined that the assessee-company had not operated as a mutual concern, there would be no question of extending exemption from tax liability. Be that as it may, to support an alternative claim for exemption, the assessee-company took a plea in the written submissions that it was acting under a trust for the contributors, and was under an overriding obligation to spend the amounts received for advertising, marketing and promotional activities. It is urged that once the incoming amount is earmarked for an obligation, it does not become "income" in the hands of the assessee as no occasion for the application of such income arises.

37 In the written submissions, the assessee-company has contended thus :

"The hon'ble High Court further erred in not adjudicating the specific ground raised by the appellant that the contributions received by the appellant cannot be said to be its income because the appellant

merely holds them as a trustee and also under an overriding obligation to spend such contributions received for AMP activities."

**38** The law on what amounts to a case of diversion before accrual and what amounts to application post accrual is well settled and can be summarised by making reference to *Dalmia Cement Ltd.* v. *CIT*[1], wherein the following extract of *CIT* v. *Sitaldas Tirathdas*[2] was quoted with approval[3] :

> "In our opinion, the true test is whether the amount sought to be deducted, in truth, never reached the assessee as his income. Obligations, no doubt, there are in every case, but it is the nature of the obligation which is the decisive fact. There is a difference between an amount which a person is obliged to apply out of his income and an amount which by the nature of the obligation cannot be said to be a part of the income of the assessee. Where by the obligation income is diverted before it reaches the assessee, it is deductible ; but where the income is required to be applied to discharge an obligation after such income reaches the assessee, the same consequence, in law, does not follow. It is the first kind of payment which can truly be excused and not the second. The second payment is merely an obligation to pay another a portion of one's own income, which has been received and is since applied. The first is a case in which the income never reaches the assessee, who even if he were to collect it, does so, not as part of his income, but for and on behalf of the person to whom it is payable."

Furthermore, in *Associated Power Co. Ltd.* v. *CIT*[4], this court again observed thus[5] :

> "The application of the doctrine of diversion of income by reason of an overriding title is quite inapposite. The doctrine applies when, by reason of an overriding title or obligation, income is diverted and never reaches the person in whose hands it is sought to be assessed."

Similarly, in *CIT* v. *Travancore Sugars and Chemicals Ltd.*[6], this court restated thus[7] :

> "It is thus clear that where by the obligation income is diverted before it reaches the assessee, it is deductible. But, where the income

1. [1999] 237 ITR 617 (SC) ; [1999] 4 SCC 124.
2. [1961] 41 ITR 367 (SC) ; AIR 1961 SC 728.
3. Page 374 of 41 ITR.
4. [1996] 218 ITR 195 (SC) ; [1996] 7 SCC 221.
5. Page 207 of 218 ITR.
6. [1973] 88 ITR 1 (SC) ; [1973] 3 SCC 274.
7. Page 13 of 88 ITR.

is required to be applied to discharge an obligation after such income reaches the assessee it is merely a case of application of income to satisfy an obligation of payment and is therefore not deductible."

39 The Commissioner of Income-tax (Appeals), while rejecting this ground, relied upon *Sitaldas Tirathdas* (supra), and observed thus :

". . . Where an assessee applies an income to discharge an obligation after the income reaches the hands of the assessee, it would be an application of income and this would resulting taxation of such income in the hands of the appellant."

40 We note that the same ground was also pressed in appeal before the Tribunal which finds mention in the Tribunal's order dated January 31, 2008 in the following words :

"(b) In failing to consider and appreciate that the amount received by the appellant from the franchisees towards advertising contributions are diverted at source by overriding title for being spent on advertisement."

However, the Tribunal did not record any observation addressing this ground in the abovesaid order. It has been brought to our notice that the assessee-company has made an application under section 254(2) of the 1961 Act for rectification of the Tribunal's order citing an error apparent on the face of the record. The said application is stated to be pending.

41 Considering the fact that the question of diversion by overriding title was neither framed nor agitated in the appeal memo before the High Court or before this court (except a brief mention in the written submissions), coupled with the fact that neither the Tribunal nor the High Court has dealt with that plea and that the rectification application raising that ground is still undecided and stated to be pending before the Tribunal, we deem it appropriate to leave it open to the appellant to pursue the rectification application, if so advised. We may not be understood to have expressed any opinion either way as regards the tenability of the said application or otherwise.

42 In view of the aforestated terms, the questions posed for our consideration stand answered against the appellant (assessee-company) and in favour of the Revenue and the appeal stands disposed of upholding the impugned judgment with liberty to the appellant to pursue remedy of rectification, as per law. There shall be no order as to costs. Pending interlocutory applications, if any, shall also stand disposed of.

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**[2020] 424 ITR 664 (SC)**

[IN THE SUPREME COURT OF INDIA]

**VODAFONE IDEA LTD.**

(earlier known as Vodafone Mobile Services Ltd.)

***v.***

**ASSISTANT COMMISSIONER OF INCOME-TAX AND ANOTHER**

**UDAY UMESH LALIT** and **VINEET SARAN** JJ.

April 29, 2020.

**SS ▸ ITA 1961, ss 143(1), (1D), (2), 241A**
**AY ▸ 2014-15 to 2017-18**
**HF ▸ Department/Assessee**

ASSESSMENT—RETURNS—PROCESSING—REFUNDS—RETURN CLAIMING REFUND—POWER TO DECLINE PROCESSING OF—PRIMA FACIE ADJUSTMENTS—ASSESSMENT PURSUANT TO SCRUTINY NOTICE—DISTINCTION BETWEEN—PROCESSING OF RETURN WHETHER PERMISSIBLE AFTER SCRUTINY NOTICE—ASSESSEE CANNOT INSIST THAT PROCESSING BE COMPLETED AND REFUND MADE BEFORE COMPLETION OF ASSESSMENT PURSUANT TO SCRUTINY NOTICE—WHERE NOTICE ISSUED AND PROCEEDINGS INITIATED, PROCESSING OF RETURN "SHALL NOT BE NECESSARY" FOR ASSESSMENT YEARS ENDING ON MARCH 31, 2017 OR BEFORE—ISSUANCE OF NOTICE ITSELF SUFFICIENT—NO SEPARATE INTIMATION THAT REFUND WITHHELD PENDING SCRUTINY ASSESSMENT CONTEMPLATED—CHANGE OF LAW—ASSESSMENT YEARS COMMENCING ON OR AFTER APRIL 1, 2017—CONDITIONS TO BE SATISFIED BEFORE REFUSING REFUND UNDER SECTION 143(1D)—SEPARATE RECORDING OF SATISFACTION BY ASSESSING OFFICER THAT REFUND LIKELY TO ADVERSELY AFFECT REVENUE AND PREVIOUS APPROVAL OF PRINCIPAL COMMISSIONER OR COMMISSIONER NECESSARY—INCOME-TAX ACT, 1961, SS. 143(1), (1D), (2), 241A.

*Sub-section (1D) was inserted in section 143 of the Income-tax Act, 1961 by the Finance Act, 2012 to provide that processing of returns will not be necessary in cases where notice under sub-section (2) of section 143 has been issued for scrutiny of the return. With effect from April 1, 2017, sub-section (1D) and its proviso provide that with effect from assessment year 2017-18, processing under section 143(1) of the Act is to be done before the passing of the assessment order and that the provisions of the sub-section shall cease to apply in respect of returns furnished for assessment year 2017-18 and onwards. A new section 241A was also inserted to provide that, for the*

*returns furnished for assessment year commencing on or after April 1, 2017, where refund of any amount becomes due to the assessee under section 143(1) of the Act and the Assessing Officer is of the opinion that grant of refund may adversely affect the recovery of revenue, he may, for reasons recorded in writing and with the previous approval of the Principal Commissioner or Commissioner, withhold the refund up to the date on which the assessment is made.*

*Clause (a) of sub-section (1) of section 143 has six sub-clauses specifying the kinds of adjustments which are required to be made for computing the total income or loss. Upon causing such adjustments after due intimation or notice to the assessee, the element of tax, interest and fee is to be computed in terms of clause (b). Thereafter, in terms of clause (c), due credit to the amount of tax paid and any relief that is allowable is to be given and the net amount payable or to be refunded, is to be computed. The intimation to be generated under clause (d) is on the basis of such exercise and if any refund is due, it has to be granted in terms of clause (e). Thus, at every stage in sub-section (1) the return submitted by the assessee forms the foundation, with respect to which, if any of the inconsistencies referred to in various sub-clauses of clause (a) are found, appropriate adjustments are to be made. On the other hand, the exercise of power under sub-section (2) of section 143 of the Act, leading to the passing of an order under sub-section (3) thereof, is to be undertaken where it is considered necessary or expedient to ensure that the assessee has not understated the income, or has not computed excessive loss, or has not underpaid the tax in any manner. The issuance of notice and consequent proceedings are premised on any of these three postulates. In other words, the return filed by the assessee itself calls for or requires a further probe and deeper consideration. Upon issuance of notice, the assessee is entitled to produce evidence in support of his case. After hearing the assessee and considering the evidence so produced, by an order in writing, assessment of total income or loss is to be made.*

*The nature of exercise of power under sub-section (1) as against that under sub-sections (2) and (3) is thus completely different. In the former case, the matter is processed, only to check whether any apparent inconsistencies are evident on the face of the return and connected material which may call for any adjustment while in the latter case, the matter is scrutinised after taking into account such evidence as the assessee may produce. The exercise in the latter case is to ensure that there is no understating of income or overstating of loss or underpayment of the tax in any manner. In other words, the*

*veracity of the return is checked threadbare rather than considering mere apparent inconsistencies from the return.*

*The dimension of power under sub-sections (2) and (3) of section 143 of the Act is far greater and deeper than mere adjustments to be made in respect of what is available from the return. Once such scrutiny is undertaken and proceedings are initiated by issuance of a notice under sub-section (2) of section 143, it would be anomalous and incongruent that while such proceedings so initiated are pending, the return be processed under sub-section (1) of section 143, which may in a given case, entail payment of refund. Logically, the outcome of the exercise initiated through notice under sub-section (2) of section 143, must determine whether any refund is due and payable. If the return itself is under probe and scrutiny, such return cannot be the foundation to sustain a claim for refund till such scrutiny is complete. Considering the nature of power exercisable under these two limbs of section 143, the inescapable conclusion is that the processing of the return under sub-section (1) of section 143 must await the further exercise of power of scrutiny assessment under sub-sections (2) and (3) of section 143. If the power under sub-section (2) of section 143 of the Act is initiated in a manner known to law, there cannot be any insistence that the processing under sub-section (1) of section 143 be completed and refund be made before the scrutiny pursuant to notice under sub-section (2) of section 143 is over.*

*This conclusion is fortified and strengthened by clear stipulation to that effect in sub-section (1D) of section 143. The legislative intent is clear from the expression, "the processing of a return shall not be necessary, where a notice has been issued to the assessee under sub-section (2)" and by use of the non obstante clause. Though the period for which it would not be necessary to process the return was sought to be specified by the Finance Act, 2016, the mere absence of such period in the provision as it stands today, makes no difference. The intent of Parliament is that in cases where notice under sub-section (2) is issued and proceedings are initiated, the processing of a return under sub-section (1) shall not be necessary. The intent to have the general principle emanating from sub-section (1) of section 143 overridden, in cases where proceedings are initiated pursuant to notice under sub-section (2) of the Act, is emphasised by use of the non obstante clause in sub-section (1D) and the expression "it shall not be necessary". Therefore, in respect of assessment years ending on March 31, 2017 or before, if a notice was issued in conformity with the requirements stated in sub-section (2) of section 143 of the Act, it shall not be necessary to process the refund under sub-section (1) of*

*section 143 of the Act and the requirement to process the return shall stand overridden.*

VAISHALI ABHIMANYU JOSHI *v.* NANASAHEB GOPAL JOSHI [2017] 14 SCC 373 *applied.*

*Issuance of notice under sub-section (2) itself is sufficient indication that the matter is being considered from the perspective whether there is any avoidance of tax in any manner. Sub-section (1D) of section 143 of the Act does not contemplate either issuance of any such intimation or further application of mind that the processing must be kept in abeyance. It would not, therefore, be proper to read into the provision the requirement to send a separate intimation. Issuance of notice under sub-section (2) of section 143 is enough to trigger the required consequence. No other intimation is either contemplated by the statute to achieve any purpose.*

*However, in respect of assessment years commencing on or after April 1, 2017, section 241A of the Act requires a separate recording of satisfaction on the part of the Assessing Officer that having regard to the fact that a notice has been issued under sub-section (2) of section 143, the grant of refund is likely to adversely affect the Revenue ; whereafter, with the previous approval of the Principal Commissioner or Commissioner and for reasons to be recorded in writing, the refund can be withheld. Since the statute envisages exercise of power of withholding of refund in a particular manner for assessment years commencing after April 1, 2017 the requirements of section 241A of the Act must be satisfied.*

*For assessment years 2014-15 and 2015-16, the assessee filed its returns claiming refunds of Rs. 1532.09 crores, Rs. 1355.51 crores and Rs. 1128.47 crores respectively. The assessee filed revised returns of income pertaining to the assessment year 2014-15 and the assessment year 2015-16 on March 31, 2016 and November 25, 2016 respectively, claiming refunds of Rs. 1,532.09 crores and Rs. 1,355.51 crores, respectively. It filed its return for the assessment year 2016-17, claiming refund of Rs. 1,128.47 crores on November 30, 2016. Subsequently, in view of the advance pricing agreement dated November 18, 2016 entered into with the Central Board of Direct Taxes under section 92CC of the Act, it filed a modified return for the assessment year 2014-15 on February 22, 2017. Notices under section 143(2) of the Income-tax Act, 1961 were issued to the assessee within the specified time in respect of these assessment years. By letters dated July 24, 2017 and September 19, 2017, the assessee communicated to the Department that it was under immense financial stress and, therefore, the returns should be processed forthwith. It filed its return for the assessment year 2017-18 on November 25, 2017 claiming a*

*refund of Rs. 743.67 crores. On the ground that there was complete inaction on the part of the Department in processing the returns filed by the assessee and in issuing appropriate refunds to the assessee, the assessee filed a writ petition. During the pendency of the writ petition, the Assistant Commissioner issued a letter dated July 23, 2018 stating that exercising the powers under sections 143(1D) and 241A of the Act, the processing of returns under section 143(1) was declined. In the meantime, a revised return was filed by the assessee for assessment year 2017-18 claiming refund of Rs. 744.94 crores. Notice under section 143(2) was issued thereafter for this year. On March 14, 2019 an intimation was sent to the assessee by the Assistant Commissioner stating that refund for the assessment year 2017-18 had been withheld till the completion of scrutiny proceedings under section 143(3) or 144C of the Act. For the assessment years 2014-15 and 2015-16, the assessee's objections against the draft assessment orders were disposed of and final assessment orders under section 143(3) of the Act were passed on October 31, 2019, holding the assessee entitled to refund of Rs. 733 crores (approximately) in respect of assessment year 2014-15, and raising a demand in the sum of Rs. 582 crores (approximately) for assessment year 2015-16. In an appeal preferred by the assessee, the demand for assessment year 2015-16 was stayed by the Appellate Tribunal. The High Court dismissed the writ petition. On appeal to the Supreme Court :*

Held, *(i) that the Department had conceded that the order dated July 23, 2018 passed under section 143(1D) of the Act in respect of assessment year 2017-18 was without jurisdiction, as by that time no order under section 143(2) of the Act for that assessment year had been passed. In the circumstances, a fresh order was passed on March 14, 2019 after due compliance with the statutory requirements. The record showed that all the antecedent steps leading to the order were taken in accordance with law and settled practice : the intimation under section 143(1) was sent to the e-mail address provided by the assessee, and the intimation stated that refund determined under section 143(1) in the intimation was withheld in terms of the proviso to section 241A and that the refund if any would be released on completion of the assessment under section 143(3)/144(4) as the case may be, with interest under section 244A and subject to adjustment of arrears demand, if any under section 245.*

*(ii) That the submission that the intimation dated July 23, 2018 must be held to be invalid, inter alia, on the ground that it was issued well after the period within which the return was required to be processed under sub-section*

*(1) of section 143 of the Act, was not tenable, in respect of assessment years 2014-15 to 2016-17.*

*(iii) That in terms of the second proviso to sub-section (1) of section 143 of the Act, the required intimation under the sub-section must be given before the expiry of one year from the end of the financial year in which the return is made. In respect of the assessment year 2017-18, the return having been filed on November 25, 2017, the period available in terms of the second proviso was up to March 31, 2019, without taking into account the fact that a revised return was filed on July 13, 2018. The exercise of power on March 14, 2019 was not only after issuance of notice under sub-section (2) of section 143 and after recording due satisfaction in terms of section 241A of the Act, but was also well within the period contemplated by sub-section (1) of section 143 of the Act for causing due intimation.*

*(iv) That whether the satisfaction recorded in terms of section 241A of the Act was otherwise correct or not and whether or not a case for withholding of refund was made out, were not issues for consideration by the court. There was nothing in the exercise of power that led to the passing of the order dated March 14, 2019 which could be said to have violated any statutory requirements.*

*(v) That for assessment year 2014-15 the final assessment order passed under section 143(3) of the Act indicated that the assessee was entitled to refund of Rs. 733 crores, while for assessment year 2015-16 there was a demand for Rs. 582 crores.*

*[The court directed refund of the amount of Rs. 733 crores within four weeks subject to any proceedings that the Department may deem appropriate to initiate in accordance with law. The court also directed the Department to conclude the proceedings initiated pursuant to notices under sub-section (2) of section 143 of the Act in respect of assessment years 2016-17 and 2017-18 as early as possible.]*

*Decision of the Delhi High Court in* VODAFONE MOBILE SERVICES LTD. *v.* ASST. CIT [2020] 421 ITR 193 (Delhi) *affirmed subject to directions.*

Cases referred to :

Brij Kishore Sharma *v.* Ram Singh and Sons [1996] 11 SCC 480 (para 16)

CIT *v.* Gujarat Electricity Board [2003] 260 ITR 84 (SC) (para 8)

CIT (Deputy) *v.* Zuari Estate Development and Investment Co. Ltd. [2015] 373 ITR 661 (SC) (para 3)

Group M. Media India (P.) Ltd. *v.* Union of India [2016] 388 ITR 594 (Bom) (para 3)

Gujarat Poly-AVX Electronics Ltd. *v.* Deputy CIT (Asstt.) [1996] 222 ITR 140 (Guj) (para 8)

Mohd. Ibrahim *v.* State Transport Appellate Tribunal [1970] 2 SCC 233 (para 16)

Rasammal Issetheerammal Fernandez, etc. *v.* Joosa Mariyam Fernandez [2000] 7 SCC 189 (para 16)

Sohanlal *v.* Amin Chand and Sons [1973] 2 SCC 608 (para 16)

Tata Teleservices Ltd. *v.* CBDT [2016] 386 ITR 30 (Delhi) (para 3)

Union of India *v.* G. M. Kokil [1984] Supp. SCC 196 (para 17)

Upper India Cable Co. *v.* Bal Kishan [1984] 3 SCC 462 (para 16)

Vaishali Abhimanyu Joshi *v.* Nanasaheb Gopal Joshi [2017] 14 SCC 373 (para 17)

Vodafone Mobile Services Ltd. *v.* Asst. CIT [2020] 421 ITR 193 (Delhi) (para 2)

**Civil Appeal No. 2377 of 2020.**

Appeal from the judgment and order dated December 14, 2018 of the Delhi High Court in Writ Petition (Civil) No. 2730 of 2018. The judgment of the High Court is reported as *Vodafone Mobile Services Ltd.* v. *Asst. CIT* [2020] 421 ITR 193 (Delhi).

*J. D. Mistri,* Senior Advocate, (*Ms. Anuradha Dutt, Ms. Fereshte D. Sethna, Sachit Jolly, Rohit Garg, Siddharth Joshi* and *Ms. B. Vijayalakshmi Menon*, Advocates, with him) for the appellant.

*Mr. Zoheb Hossain, Saurabh Mishra, Piyush Goyal, Vivek Gurnani* and *Mrs. Anil Katiyar*, Advocates, for the respondent.

**JUDGMENT**

The judgment of the court was delivered by

1 UDAY UMESH LALIT J.—Leave granted.

2 This appeal arises out of the final judgment and order dated December 14, 2018 passed by the High Court[1] in Writ Petition (Civil) No. 2730 of 2018[2] preferred by the appellant herein.

3 The facts leading to the filing of this appeal, in brief, are as under :

(A) The appellant-Vodafone Idea Ltd. (earlier known as Vodafone Mobile Services Ltd. or VMSL for short) is engaged in providing telecommunication services in different circles.

1. The High Court of Delhi at New Delhi.
2. *Vodafone Mobile Services Ltd.* v. *Asst. CIT* [2020] 421 ITR 193 (Delhi).

(a) By amalgamation which came into effect on April 1, 2011, four group entities : Vodafone Cellular Ltd., Vodafone Digilink Ltd., Vodafone East Ltd. and Vodafone South Ltd. got merged in VMSL.

(b) By second scheme of amalgamation, two other group entities : Vodafone Spacetel Ltd. and Vodafone West Ltd. got merged in VMSL with effect from April 1, 2012.

(c) While the proceedings in the instant case were pending, by scheme of arrangement[1] between VMSL and Idea Cellular Ltd. Vodafone Idea Ltd. — the resultant company assumed all the rights and liabilities of the amalgamating/transferor companies.

Most of the factual developments in the matter, as set out hereafter, were before the said scheme of arrangement.

(B) For the assessment year[2] 2014-15, the appellant filed income-tax return (ITR, for short) on September 30, 2014 claiming refund of Rs. 1532.09 crores. On August 31, 2015, a notice under section 143(2) of the Act[3] was issued to the appellant in respect of the assessment year 2014-15. On November 1, 2015, the appellant filed income-tax return for the assessment year 2015-16 claiming refund of Rs. 1355.51 crores. A notice under section 143(2) of the Act was issued by the Department on March 16, 2016 in respect of the assessment year 2015-16. A revised return was filed by the appellant on March 31, 2016 in respect of the assessment year 2014-15. The appellant entered into an advanced pricing agreement with the CBDT[4] under section 92CC of the Act. Thereafter, further revised return was filed on November 25, 2016 for the assessment year 2015-16 and a modified return in terms of section 92CD of the Act was filed by the appellant on February 22, 2017 for the assessment year 2014-15.

(C) For the assessment year 2016-17, the appellant filed income-tax return on November 30, 2016 claiming refund of Rs. 1128.47 crores. A notice under section 143(2) of the Act was issued to the appellant on July 3, 2017 for the assessment year 2016-17.

(D) For the assessment year 2017-18, income-tax return was filed by the appellant on November 25, 2017 claiming refund of Rs. 743 crores.

(E) Submitting that there was complete inaction on part of the respondents in processing the income-tax returns filed by the appellant

1. Formulated by the order dated January 2018 passed by National Company Law Tribunal, Mumbai and order dated January 11, 2018 by National Company Law Tribunal, Ahmedabad.
2. The assessment year.
3. The Income-tax Act, 1961.
4. Central Board of Direct Taxes.

and in issuing appropriate refund to the appellant, Writ Petition (Civil) No. 2730 of 2018 was filed by the appellant in the High Court, praying for following principal relief.

"a. Writ of mandamus or writ, order or direction in the nature of mandamus, or any other appropriate writ, order or direction under article 226/227 of the Constitution of India directing the respondents to process and grant refunds for the assessment years 2014-15 to 2017-18, along with interest under section 244A of the Act ;"

(F) On July 3, 2018, respondent No.1 filed an affidavit-in-reply submitting, inter alia, that the income-tax returns of the appellant raised multiple issues like transfer pricing adjustment, capitalization of licence fees, 3G spectrum fees, asset restoration cost obligation including the effect of amalgamation of group entities which required thorough scrutiny and determination.

(G) During the pendency of the said writ petition, a letter was issued by respondent No. 1 on July 23, 2018, the relevant portion of which was as under :

"The assessment years for which request has been made to process the return under section 143(1) are already under scrutiny for the assessment year 2012-13, the assessment year 2013-14, the assessment year 2014-15, the assessment year 2015-16 and the assessment year 2016-17. I would like to draw your attention to section 143(1D) of the Income-tax Act :

(1D) Notwithstanding anything contained in sub-section (1), the processing of a return shall not be necessary, where a notice has been issued to the assessee under sub-section (2). The case is under compulsory scrutiny for the assessment year 2017-18 and as per section 241A of the Income-tax, Act 1961 :

'For every assessment year commencing on or after the 1st day of April, 2017, where refund of any amount becomes due to the assessee under the provisions of sub-section (1) of section 143 and the Assessing Officer is of the opinion, having regard to the fact that a notice has been issued under sub-section (2) of section 143 in respect of such return, that the grant of the refund is likely to adversely affect the Revenue, he may, for reasons to be recorded in writing and with the previous approval of the Principal Commissioner or Commissioner, as the case may be, withhold the refund up to the date on which the assessment is made.'

Considering, pending special audit, pending scrutiny, pending demands of amount of more than 4500 crores, it will be prejudicial to the interests of the Revenue to process the returns without completion of the pending scrutiny cases. Therefore, exercising the powers under section 143(1D) of the Income-tax Act, 1961 and under section 241A of the Income-tax Act, 1961, the undersigned decline the processing of returns under section 143(1). The above decision has been taken after taking into cognizance the order of the honourable High Court of Delhi in *Tata Teleservices Limited* v. *CBDT* dated May 11, 2016[1] in para 24 of the judgment : 'The question whether such return should be processed will have to be decided by the Assessing Officer concerned exercising his discretion in terms of section 143(1D) of the Act'."

(H) In the meantime, on July 13, 2018 a revised return was filed by the appellant for the assessment year 2017-18 claiming refund of Rs. 744.94 crores. A notice under section 143(2) of the Act was issued to the appellant on August 10, 2018 for the assessment year 2017-18.

(I) On August 31, 2018, VMSL merged with Idea Cellular Ltd. and the resultant company was named Vodafone Idea Ltd.

(J) By its judgment and order dated December 14, 2018, the High Court dismissed the said writ petition.

(J-1) The submissions of the appellant were recorded as under[2] :

"Vodafone also place reliance on the decision of this court in *Tata Teleservices Ltd.* v. *CBDT* [2016] 386 ITR 30 (Delhi) and Bombay High Court in *Group M. Media India (P.) Ltd.* v. *Union of India* 2016 SCC OnLine Bom 13624[3], which held that the return should be processed within a year and only where the Assessing Officer is of the view that issuance of refund would be detrimental to collection of demands which may arise, he may invoke the provision of section 143(1D) of the Act . . .

With respect to the delay in processing of the tax return, Vodafone places reliance on the decision of this court in *Tata Teleservices Limited* v. *CBDT* (supra), and the decision of the Bombay High Court in *Group M Media India (P.)Ltd.* v. *Union of India* (supra), where it was held that the return should be processed within a year and only where the Assessing Officer is of the view that issuance of refund would be detrimental to collection of demands that may arise, he may

1. [2016] 386 ITR 30 (Delhi).
2. Page 198 of 421 ITR.
3. [2016] 388 ITR 594 (Bom).

invoke the provisions of section 143(1D) of the Act. From the perusal of section 241A of the Act, it is evident that all tax returns are necessarily to be processed within the time period as prescribed under section 143(1) of the Act. In the instant case, it is note-worthy that the time period prescribed under section 143(1) of the Act has expired and there has been no correspondence from the Revenue that discretion under section 143(1D) was exercised. . .

It was contended that after the lapse of the one year period, by reason of second proviso to section 143(1), the right to claim refund is vested in any assessee. The counsel argued that this is independent of the Revenue's power to issue a scrutiny notice under section 143(2), for which the period of limitation is longer. However, if the Assessing Officer does not issue any notice, or intimation, if the assessee can claim refund, that right is a statutorily vested one if, within the said period of one year, a reasoned order is not made under section 143 (1D) within the said one year period."

(J-2) On the other hand, the submissions on behalf of the respondents were[1] :

"The Revenue denies allegations of deliberate omission to refund amounts aggregating to Rs. 4759.74 crores along with applicable interest and states that income-tax returns were not processed under section 143(1). The assessment years under consideration were picked up for scrutiny under section 143(3) and there is a prima facie likelihood of a substantial demand being raised by the Income-tax Department, as has been done earlier in *Vodafone's* earlier case. Further, the Revenue submitted that in *Vodafone's* own case for the assessment year 2011-12 wherein the returned loss was Rs. 33,93,397 and subsequently, the income determined by the Assessing Officer was Rs. 546,64,25,250 . . .

The counsel for the Revenue contended that for the relevant period under consideration, the Assessing Officer has already issued notice under sub-section (2) of section 143 within time. As per the then prevailing provision, it was thereafter not necessary for the Assessing Officer to proceed under sub-section (1) of section 143. Further, the learned counsel placed reliance on section 143(1D) of the Act to explain that the refund has not been processed till date. The learned counsel urged that sub-section (1D) of section 143 which starts with a non obstante clause provided that notwithstanding anything

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contained in sub-section (1), the processing of the return shall not be necessary before the expiry of the period specified in the second proviso where a notice has been issued to the assessee under section 143(2). The proviso to section 143(1D) provided that such return shall be processed before the issuance of an order under sub-section (3). Therefore, section 143(1D) overrides section 143(1). Therefore, the counsel submitted that under section 143(1D) of the Act, the processing of return shall not be necessary, where notice has been issued under section 143(2) of the Act.

The counsel placed on record letter F. No. ACIT/C-26(2)/2018-19/216 dated July 23, 2018. It is in response to the multiple communications by the assessee for expeditious processing of returns for the different assessment years. The order informs that the cases are pending for scrutiny as follows : for the assessment year 2012-13 and 2013-14, the assessment is under special audit and for the assessment year 2014-15, the assessee approached the Authority for Advance Rulings and lastly, returns for the assessment years 2015-16 and 2016-17, are under scrutiny. The assessment years for which request has been made to process the return under section 143(1) are already under scrutiny for the various assessment years. Therefore, exercising the power under section 143(1D), the Assistant Commissioner declined the processing of returns under section 143(1). Further, the case is under compulsory scrutiny for the assessment year 2017-18, exercising the power under section 241A, the Assistant Commissioner declined the processing of returns under section 143(1) . . ."

(J-3) After considering the rival submissions, relevant statutory provisions and the decisions relied upon, the High Court observed[1] :

"In the facts of the present case, the issue canvassed is on the interpretation of section 143(1D) of the Act. It is first necessary to refer to the statutory provisions and thereafter consider the effect of such provisions on Vodafone's request for refund for the said assessment years. On reading of the section 143 of the Act, it is apparent that when returns are filed either under section 139 or pursuant to a notice under section 142(1), section 143(1) mandates that the returns shall be processed in the manner prescribed in the clauses (a) to (e) thereof. The processing of a return thus involves determination of total income or loss, tax and interest, if any, payable and sum payable by, or the amount of refund due to the assessee. Section 143(1)(d)

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stipulates that an intimation shall be prepared or generated and sent to the assessee specifying the sum determined payable by, or the amount of refund due to the assessee under clause (c). Section 143(1)(e) provides that the amount of refund due in pursuance of the determination under clause (c) shall be granted to the assessee. A reading of proviso to section 143(1) reveals that it mandates that the intimation as provided in section 143(1)(d) should be issued before the expiry of one year from the end of the financial year in which the return is made. Before proceeding to section 143(1D) as it stood at the relevant time, it is essential to refer to section 143(2) and (3). Sub-section (2) contemplates issuance of a notice in the contingency covered by the said provision. Sub-section (3) provides that once such a notice is served, after following the procedure laid, the Assessing Officer is required to pass an order in writing making an assessment of the total income or loss and determine the sum payable by the assessee or refund of any amount due to him on the basis of the assessment. It is also relevant to notice that whether it is the processing of a return under section 143(1) or an order under section 143(3) is subject to the same time limit, i.e. section 153(1) . . .

A reading of the above judgments and the relevant provisions, clearly shows that section 143(2) empowers, the Assessing Officer to issue notice to the assessee to produce documents or other evidence, to prove the genuineness of the income-tax return. Under section 143(1D) of the Act an introduced by the Finance Act, 2012 processing of a return under section 143(1)(a) is not necessary where a notice has been issued under section 143(2) of the Act. This provision has now been amended by the Finance Act, 2016 (with effect from the assessment year 2017-18) to provide that if scrutiny notice is issued under section 143(2), processing of return shall not be necessary before the expiry of one year from the end of the financial year in which return is submitted.

The assessee's argument in these proceedings is that once the one year period in proviso to section 143(1) ends, the return – and whatever calculations are contained in it, with respect to tax liability as well as the consequential refunds, become final, subject to only one event, issuance of notice under section 143(2).

To this court, it appears that the net effect of *Tata Teleservices* (supra) is that the Revenue cannot be inactive, in cases where the assessee claims refund, and the one year period is over (under proviso

to section 143(1)) ends. The Assessing Officer has to apply his mind to consider whether the facts and circumstances of the case, warrant some or all of the refund of the assessee's amounts, or if all of it needs to be withheld, whenever the assessee presses for refund. This exercise should be undertaken promptly, keeping in mind the time limit under the normal provision of section 143(1) expires. This court held in *Tata Teleservices Ltd.* (supra) and the Bombay High Court in case of *Group M. Media India (P.) Ltd.* (supra) that it would be wholly inequitable for the Assessing Officer to merely sit over the petitioner's request for refund citing the availability of time up to the last date of framing the assessment under section 143(3). The proper interpretation of the statute and the situation in such a case would be, the Assessing Officer should take up an expeditious disposal of the question once the assessee requests for release of the refund . . .

Now in this case, acknowledgment or intimation had not been sent by the Assessing Officer. There is no doubt that the period of one year indicated in the second proviso to section 143(1). However, section 143(1D) begins with a non obstante clause that overbears that provision. *Tata Teleservices* (supra) and the Bombay High Court ruling in *Group M. Media India P. Ltd.* (supra) state that the fact that a regular assessment is resorted to, does not ipso facto mean that in every case, the Assessing Officer has to refuse refunds or there is an automatic bar to refunds. The Assessing Officer has to apply his mind and make an order keeping in perspective the facts of the case.

In this case, the Revenue has relied on an order dated July 28, 2018, which inter alia, stated that 'considering pending special audit, pending scrutiny, opening demands of amount more than 4500 crores, it will be prejudicial to the interests of the Revenue to process the returns without completion of the pending scrutiny cases. Therefore, exercising powers under section 143(1) and under section 241A of the Act, the undersigned decline the processing of returns under section 143(1). The senior counsel for Vodafone had attacked the reliance on this order, stating that it was made later. However, that is an aspect this court cannot go into. Facially, the order contains reasons. Therefore, unlike *Tata Teleservices*, a reasoned order was made ; that decision was based on a circular, which fettered the Assessing Officer's discretion. Therefore, the Central Board of Direct Taxes' circular was set aside . . .

As far as the argument that the expiry of the one year period, per second proviso to section 143(1) resulting in finality of the intimation

of acceptance, this court is of opinion that the deeming provision in question, i.e., section 143(1)(d) only talks of two eventualities : 'shall be deemed to be the intimation in a case where no sum is payable by, or refundable to, the assessee under clause (c), and where no adjustment has been made under clause (a)'. Secondly, that intimation or acknowledgment cannot confer any greater right than for the assessee to ask the Assessing Officer to process the refund and make over the money ; it is up to the Assessing Officer wherever the possibility of issuing a notice under section 143(2) exists, or where such notice has been issued, to apply his mind, and decide whether given the nature of the returns and the potential or likely liability, the refund can be given. It does not mean that when an assessment - pursuant to notice under section 143(2) is pending, such right to claim refund can accrue. This court also recollects the decision of the Supreme Court in *Deputy CIT* v. *Zuari Estate Development and Investment Co. Ltd.* [2015] 15 SCC 248[1] which held that an intimation under section 143(1) is not to be considered as an assessment."

(K) On December 27, 2018 and December 31, 2018, draft assessment orders in terms of section 144C of the Act were passed for the assessment year 2014-15 and the assessment year 2015-16 respectively.

(L) In the Special Leave Petition (from which this appeal arises) questioning the aforesaid decision of the High Court, notice was issued by this court on January 18, 2019. In the affidavit-in-reply, the respondents asserted :

"7. That having extracted the relevant provisions, it would be relevant to state that the petitioner itself has made several averments before the High Court that is facing 'precarious financial conditions' with an accumulated loss of Rs. 5,557 crores and debts amounting to Rs. 53,000 crores as on March 31, 2017'. It is equally pertinent to state that the respondent-Revenue had filed a counter-affidavit on July 3, 2018 against the writ petition in the High Court of Delhi wherein it has been categorically averred that there are huge pending demands against the petitioner herein more than of Rs. 5000 crores. The contents of the counter-affidavit before the High Court may be treated as a part and parcel of the present affidavit. It has been stated that multiple issues on which addition have been made giving rise to the demand liabilities, and several of such issues are also recurring in nature . . .

1. [2015] 373 ITR 661 (SC).

10. That it is also submitted that the order dated July 23, 2018 passed by the Assessing Officer is an order under section 143(1D) for the assessment years 2012-13 to 2016-17 as evident from a bare reading of the said order giving reasons for refusal of refund claimed by Vodafone Mobile Service Limited. As far as the refusal of refund claimed for the assessment year 2017-18 is concerned, the said order draws its power under section 241A of the Act as clearly stated in the order dated July 23, 2018."

Reference was made to various pending proceedings where the demands raised for earlier assessment years were stayed and it was stated :

"24. That it is wrong to say that the letter/order dated July 23, 2018 issued by respondent No. 1 under sections 143(1D) and 241A of the Income-tax Act, 1961 is beyond limitation, bereft of any cogent reasoning and without jurisdiction as the letter/order was issued for good reasons to protect the interests of the Revenue which is reflected vide para 45 of the impugned judgment. The reasoning was based upon pending special audit, pending scrutiny and pending demands of more than Rs. 5,000 crores. Further, the letter/order was not beyond limitation because section 143(1D) starts with a non obstante clause, which is over and above the provisions of section 143(1), which has been discussed in para 44 of the impugned judgment."

(M) On March 14, 2019 an intimation was sent to the appellant by respondent No.1 regarding withholding of refund for the assessment year 2017-18. It stated about the demand status for earlier assessment years as under :

| *A.Y.* | *Nature of demand* | *Amount of demand raised under section 143(3)/154* | *Amount already paid/ adjusted* | *Balance outstanding* |
|---|---|---|---|---|
| 2008-09 | Corporate tax assessment under section 143(3) | 84,91,27,579 | 10,00,00,000 | 74,91,27,579 |
| 2009-10 | Corporate tax assessment under section 143(3) | 2,42,86,76,260 | 97,36,82,990 | 1,45,49,93,270 |
| 2010-11 | Corporate tax assessment under section 143(3) | 3,36,22,76,980 | 60,00,00,000 | 2,76,22,76,980 |
| 2010-11 | Corporate tax assessment under section 143(3) | 1,65,14,76,430 | | 1,65,14,76,430 |
| 2011-12 | Corporate tax assessment under section 143(3) | 2,11,61,29,711 | | 2,11,61,29,411 |

Thereafter, it went on to state :

"It is also to be noted that earlier refund was withheld vide notesheet dated July 23, 2018 after due approval due to non-availability of proceeding of return facility in ITBA for the assessment year 2017-18 which was intimated to the assessee vide letter dated July 23, 2018. In view of the above discussion there is sufficient reason to believe that issue of refund will negatively impact the interest of the Revenue. Therefore, proposal for withhold the refund for the assessment year 2017-18 was forwarded again to Principal Commissioner of Income-tax-09, Delhi and same has been approved. Approval on note sheet was taken as well as procedure for approval through ITBA was also followed for withholding of refund which also involves approval from Principal Commissioner of Income-tax-09. The approval for withholding of refund under section 241 was taken from Principal Commissioner of Income-tax-09 which was sent through proper channel through Addl. Commissioner of Income-tax Range 26.

In view of the facts above you are hereby intimated that refund of the assessment year 2017-18 in the case of M/s. Vodafone Mobile Service Limited has been withhold under section 241A of the Income-tax Act, 1961 till the completion of scrutiny proceedings under section 143(3) or 144C read with section 143(3) of the Income-tax Act, 1961."

(N) Objections raised by the appellant against the draft assessment orders issued on December 27, 2018 and December 31, 2018 were disposed of on September 20, 2019. Thereafter, final assessment orders under section 143(3) of the Act were passed on October 31, 2019 for the assessment years 2014-15 and 2015-16, whereunder the appellant was held entitled to refund of Rs. 733 crores (approximately) in respect of the assessment year 2014-15, whereas for the assessment year 2015-16 the claim for refund was rejected and demand in the sum of Rs. 582 crores (approximately) was raised. In an appeal preferred by the appellant, said demand for the assessment year 2015-16, has, since then, been stayed by the Income-tax Appellate Tribunal.

4 The relevant dates and the factual developments as stated above, can be summarised in a tabular form as under :

| *Assessment year* | *Date of filing of income-tax return* | *Notice u/s 143(2)* | *Filing of revised return* | *Modified return in terms of section 92CD* | *Draft assessment order under section 144C* | *Order by DRP disposing of objections of the appellant against order under section 144C* | *Final assessment order u/s. 143(3)* | *Order u/s. 143 (1D)* |
|---|---|---|---|---|---|---|---|---|
| 2014-15 | 30-9-2014 (Refund : Rs. 1532 Cr Approx.) | 31-8-2015 | 31-3-2016 | 22-2-2017 | 27-12-2018 | 20-9-2019 | 31-10-2019 (Refund : Rs. 733 Cr. Approx.) | 23-7-2017 |
| 2015-16 | 1-11-2015 (Refund : Rs. 135 5 Cr Approx.) | 16-3-2016 | 25-11-2016 | | 31-12-2018 | 20-9-2019 | 31-10-2019 (Demand : Rs. 82 Cr. Approx.) | 23-7-2018 |
| 2016-17 | 30-11-2016 (Refund : Rs. 1128 Cr. Approx.) | 3-7-2017 | | | | | | 23-7-2018 |
| 2017-18 | 25-11-2017 (Refund : Rs. 745 Cr Approx.) | 10-8-2018 | 13-7-2018 | | | | | 14-3-2019 |

In this appeal, we heard Mr. J. D. Mistri, learned senior advocate for the **5**
appellant and Mr. Zoheb Hossain, learned advocate for the respondents. During the course of arguments, it was accepted by the respondents that in so far as the assessment year 2017-18 was concerned, the order dated July 23, 2018 passed under section 143(1D) of the Act was without jurisdiction, as by that time no order was passed under section 143(2) of the Act for the concerned assessment year. It was submitted that in the circumstances, a fresh order was passed on March 14, 2019 after due compliance of the statutory requirements. In order to verify the developments leading to the passing of the order dated March 14, 2019, the concerned record was summoned and perused. The court was satisfied that all the antecedent steps leading to the said order were taken in accordance with law and settled practice.

An affidavit was also filed on behalf of the respondents explaining in detail the developments leading to the passing of the order dated March 14, 2019 and issuance of intimation dated April 9, 2019. It was stated :

"That as per CPC accounting of the return was completed on April 9, 2019 and intimation under section 143(1) was generated on April 9, 2019. It is also evident from page 1 of the intimation dated April 9, 2019 that contrary to the allegations of the petitioner that the intimation under section 143(1) was never communicated to them, it is submitted that the intimation under section 143(1) was sent to the e-mail address provided by the assessee, that is, atul.goel@vodafoneidea.com.

That it was in this background that the screen-shot relied upon by the assessee during the course of the hearing shows that the income-tax return was processed on April 9, 2019.

The intimation under section 143(1) was made on April 9, 2019 and the said intimation stated that refund determined under section 143(1) has been withheld as per the proviso to section 241A and that the refund if any will be released on completion of the assessment under section 143(3)/144(4) as the case may be along with the interest under section 244A and subject to adjustment of arrears demand, if any under section 245.

In view of the above, it is submitted that the CPC has adopted the due process prescribed by the ITBA-ITR Processing Instruction No. 5 dated December 14, 2018. As per the said process, the refund determination is complete immediately after recommendation of the total income-tax and matching of tax credits is completed at CPC system. At this stage the refund determination is communicated by CPC, Bangalore to Assessing Officer through the ITBA module. Once the refund is approved/withheld/blocked by the Assessing Officer, CPC will complete the accounting of the record and act according to other processes involved like section 245 of the Income-tax Act, i.e., adjustment of refund determined against tax arrears due."

5.1 One more development must also be adverted to. In the hearing dated January 8, 2020, reliance was placed on the order dated December 28, 2019 passed in connection with M/s. Idea Cellullar Ltd. It was therefore observed by this court :

"During the course of hearing, Mr. Zoheb Hossain, learned counsel appearing for the Revenue produced a copy of the order dated December 28, 2019 passed in connection with Idea Cellular Limited (with which entity the appellant now stands merged).

Mr. Hossain submitted that the order dated December 28, 2019 will have bearing on the issue in so far as the refund payable to the present appellant in respect of the assessment year 2014-15 is

concerned. We direct the Department to place on record copy of the order along with such submission as the Department wishes to place on record. Let the submissions by way of an affidavit be filed within seven days from today.

The appellant shall have liberty to respond to those submissions within next seven days."

The copy of the order dated December 28, 2019 placed on record indicates that for the assessment year 2016-17 a demand in the sum of Rs. 2824.99 crores has been raised against the appellant.

After conclusion of oral hearing, the parties also filed their written submissions.

It was submitted by the appellant : 6

"In the facts of the present case, admittedly, for the assessment years 2014-15 to 2016-17 (for which provisions of section 143(1D) of the Act are relevant), the respondent has neither processed the return of income for the said years by the last date, viz., March 31, 2018 nor did the respondent exercise the discretion provided under section 143(1D) of the Act by that. As per the respondents' own submission, such discretion under section 143(1D) of the Act was only exercised vide letter/order dated July 23, 2018, which admittedly is beyond the limitation period.

Therefore, the exercise of such discretion, having been made beyond limitation is a nullity in the eyes of law and, hence, no cognizance can be taken of such a letter/order. In so far as the assessment year 2017-18 is concerned, the respondents during the course of arguments, before this hon'ble court have admitted that order dated July 23, 2018 was without jurisdiction because on that date, neither the return of income was processed, nor a notice under section 143(2) issued, warranting exercise of powers under section 241A of the Act. On that ground alone, the impugned order in so far as the assessment year 2017-18 is concerned should be set aside and the refund claimed for that year should be granted with interest . . .

Having admitted that the order dated July 23, 2018 was without jurisdiction, the respondent set up an alternate case that the time limit for processing the return of income expires on March 31, 2020 and, therefore, the proceedings for the assessment year 2017-18 are inchoate and no direction may be issued for that year. When it was pointed out that processing has already been completed vide intimation dated April 9, 2019, the respondent changed its stand and argued

that a letter dated March 14, 2019 was issued after filing of the counter-affidavit before this hon'ble court on March 6, 2019, seeking to again exercise powers under section 241A of the Act. Admittedly, as per the e-filing portal of the Income-tax Department, and the intimation produced by the respondent before this hon'ble court on January 8, 2020, the processing of the return for the assessment year 2017-18 was completed only on April 9, 2019 and, therefore, the alleged exercise of power under section 241A on March 14, 2019 is without jurisdiction since it suffered from the same vice as the order dated July 23, 2018, i.e., refunds could not have been withheld under section 241A prior to processing of the return of income . . .

Without prejudice to the submission that the order dated July 23, 2018 issued for the assessment years 2014-15 to 2016-17 was without jurisdiction, having been issued beyond limitation and the orders dated July 23, 2018 and March 14, 2019 invoking jurisdiction under section 241A of the Act for the assessment year 2017-18 have no sanctity of law since the sine qua non for invoking that section, i.e., processing of return was completed on April 9, 2019, even on merits, neither the order dated July 23, 2018 nor the order dated March 14, 2019 disclose any grounds on which powers under section 143(1D) or section 241A of the Act could have been invoked."

7 The respondents submitted :

"On merits, it is submitted that if the Assessing Officer issued a notice under section 143(2) within the time limit, i.e., 6 months from the end of the financial year in which return was filed, then there is no longer a requirement to process the return under section 143(1). That being the position of law laid down by the hon'ble Supreme Court, the discretion under section 143(1D) can be exercised at any point prior to the passing of the final assessment order.

The entire objective of not processing a return after issuance of a scrutiny notice is that in cases where there is a likelihood of substantial demands, there should not be a compulsion on the Revenue to issue refunds. There is no anomaly in the above legislative scheme which warrants dilution of the non obstante clause and to read into section 143(1D) a limitation which the Legislature has not prescribe . . .

It is well settled that a non obstante clause is a legislative device which is employed to give overriding effect to some or all contrary provisions and as such, the operation of a non obstante clause cannot be limited in any manner and must be given its full effect . . .

The High Court at para 44 has categorically held that since section 143(1D) begins with a non obstante clause, it will overbear/override the second proviso to section 143(1) which contains a limitation period of one year for precession of return.

Without prejudice to the submission that the merits of the order dated July 23, 2018 as well as order dated March 14, 2019 has never been assailed by the petitioner before any forum, nor any arguments advanced during the hearing before the High Court and that the same cannot be raised for the first time before this hon'ble court in an SLP, it is submitted that the Assessing Officer had withheld refund in all these years for cogent and valid reasons, in the interests of the Revenue, subject to final scrutiny assessment proceedings. It is submitted that the scope of judicial review against such an order where the Assessing Officer has exercised his discretion would be limited and any interference can only be done if such an exercise of power is either wholly capricious or without any valid reasons."

The inter-relation between sub-sections of section 143 of the Act, as the section then stood, was subject matter of discussion by this court in *CIT* v. *Gujarat Electricity Board*[1] which in turn referred to the decision of the Gujarat High Court in *Gujarat Poly-AVX Electronics Ltd.* v. *Deputy CIT (Asstt.)*[2]. This court observed[3] : **8**

"The learned counsel appearing for the respondents have pointed out that in a number of judgments several High Courts have consistently taken the view that once regular assessment proceedings have commenced under section 143(2) of the Income-tax Act, 1961, it is a limitation on the jurisdiction of the Assessing Officer to commence proceedings under section 143(1)(a) of the Act.

Even, otherwise, the view taken by the Gujarat High Court seems to be correct on principle. There is no dispute that section 143(1)(a) of the Act enacts a summary procedure for quick collection of tax and quick refunds. Under the scheme if there is a serious objection to any of the orders made by the Assessing Officer determining the income, it is open to the assessee to ask for rectification under section 154. Apart therefrom, the provisions of section 143(1)(a)(i) indicate that the intimation sent under section 143(1)(a) shall be without prejudice to the provisions of sub-section (2). The Legislature, therefore, intended that where the summary procedure under sub-section (1)

1. [2003] 260 ITR 84 (SC).
2. [1996] 222 ITR 140 (Guj).
3. Page 85 of 260 ITR.

has been adopted, there should be scope available for the Revenue, either suo motu or at the instance of the assessee to make a regular assessment under sub-section (2) of section 143. The converse is not available ; a regular assessment proceeding having been commenced under section 143(2), there is no need for a summary proceeding under section 143(1)(a)."

8.1 The facts and relevant submissions in *Gujarat Poly Avx Electronics Ltd.* were recorded in the decision of the Gujarat High Court as under[1] :

"On September 12, 1994 the assessee submitted a return of loss of Rs. 1,74,78,530 for the assessment year 1993-94 as per the computation of income and depreciation chart annexed to the petition at annexure A. The assessee claimed depreciation of Rs. 1,74,78,526. Manufacturing activities started on March 24, 1993, i.e., during the accounting year ending on March 31, 1993 (the assessment year 1993-94). It was specifically pointed out that 'the amount of interest received during the public issue of Rs. 1,07,85,590 is not to be considered as income and has been given set off against the interest outgoings included under pre-operative expenditure' in view of several decisions including that of the apex court.

As stated by the learned counsel, on filing of the return, the Assessing Officer (AO) under the new scheme for assessment under section 143 of the Act, had two options ; i.e., (i) either to accept the return under section 143(1) with necessary adjustments, if there is any, or (ii) to proceed to make assessment under section 143(3) or under section 144 by issuing notice under section 143(2) of the Act. In the instant case, instead of accepting the return under section 143(1) of the Act, undisputedly, the Assessing Officer issued notice under section 143(2) of the Act on December 1, 1994, vide Annexure C. It is contended in the petition that in continuation of the notice the Assessing Officer addressed a letter on November 15, 1995 calling upon the assessee to attend on November 27, 1995, vide letter Annexure C-1. The assessee's representative appeared before the Assessing Officer on November 27, 1995 but the Assessing Officer adjourned the case to December 1, 1995. On December 1, 1995 there was a discussion between the representative of the assessee and the Assessing Officer. The assessee was called upon to make clarifications regarding various points and was also asked to clarify as to how the depreciation as claimed should not be disallowed and why interest

1. Page 142 of 222 ITR.

should not be taxed as receipt on the revenue account. It is contended by the assessee that the Assessing Officer was in the midst of the proceedings under section 143(3) of the Act. However, Assessing Officer issued intimation/order under section 143(1)(a) of the Act, vide annexure D, rejecting the return of income as computed by the assessee resulting in disallowing depreciation as claimed and by taxing the interest income of Rs. 1,07,85,590 as income from other sources and thus raised the demand of Rs. 1,30,83,741 under various heads and sections of taxes, surcharge and additional tax under sections 143(1A), 234A and 234B.

Mr. Shah, learned counsel appearing for the assessee, has contended that once the Assessing Officer has exercised an option to proceed under section 143(3) of the Act by issuing notice under section 143(2) of the Act even if adjustments that may be made by the Assessing Officer are in order, the Assessing Officer has forfeited the authority to act under section 143(1) by virtue of his having exercised option to make an assessment under section 143(3) of the Act by issuing a notice under section 143(2) of the Act.

As against this, Mr. Shelat, learned counsel has contended that it is open for the Assessing Officer to follow the procedure under section 143(1) and 143(2) simultaneously. His contention is that it is open to have parallel proceedings and it is not compulsory to assess as per section 143(3) of the Act though notice under section 143(2) of the Act is issued and before making assessment under section 143(3) of the Act he can proceed under section 143(1) of the Act. No other contention is raised."

8.1.1 The relevant provision, namely section 143 as it then stood was quoted in paragraph 6 as under[1] :

"It would be better to have a look at the relevant section which is reproduced as under :

'143(1)(a) Where a return has been made under section 139, or in response to a notice under sub-section (1) of section 143,—

(i) If any tax or interest is found due on the basis of such return, after adjustment of any tax deducted at source, any advance tax paid and any amount paid otherwise by way of tax or interest, then, without prejudice to the provisions of sub-section (2), an intimation shall be sent to the assessee specifying the sum so payable, and such

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intimation shall be deemed to be a notice of demand issued under section 156 and all the provisions of this Act shall apply accordingly ;

(ii) If any refund is due on the basis of such return, it shall be granted to the assessee :

Provided that in computing the tax or interest payable by, or refundable to the assessee, the following adjustments shall be made in the income or loss declared in the return, namely—

(i) any arithmetical errors in the return, accounts or documents accompanying it shall be rectified ;

(ii) any loss carried forward, deduction, allowance or relief, which, on the basis of the information available in such return, accounts or documents, is prima facie admissible but which is not claimed in the return, shall be allowed ;

(iii) any loss carried forward, deduction, allowance or relief claimed in the return, which, on the basis of the information available in such return, accounts or documents, is prima facie inadmissible, shall be disallowed :

Provided further that where adjustments are made under the first proviso, an intimation shall be sent to the assessee, notwithstanding that no tax or interest is found due from him after making the said adjustments :

Provided also that an intimation for any tax or interest due under this clause shall not be sent after the expiry of two years from the end of the assessment year in which the income was first assessable . . .

(1A)(a) Where as a result of the adjustments made under the first proviso to clause (a) of sub-section (1)—

(i) the income declared by any person in the return is increased ; or

(ii) the loss declared by such person in the return is reduced or is converted into income,

the Assessing Officer shall,—

(A) in a case where the increase in income under sub-clause (i) of this clause has increased the total income of such person, further increase the amount of tax payable under sub-section (1) by an additional income-tax calculated at the rate of twenty per cent on the difference between the tax on the total income so increased and the tax that would have been chargeable had such total income been reduced by the amount of adjustments and specify the additional income-tax

in the intimation to be sent under sub-clause (i) of clause (a) of sub-section (1) ;

(B) in a case where the loss so declared is reduced under sub-clause (ii) of this clause or the aforesaid adjustments have the effect of converting that loss into income, calculate a sum (hereinafter referred to as additional income-tax) equal to twenty per cent of the tax that would have been chargeable on the amount of the adjustments as if it had been the total income of such person and specify the additional income-tax so calculated in the intimation to be sent under sub-clause (i) of clause (a) of sub-section (1) ;

(C) where any refund is due under sub-section (1), reduce the amount of such refund by an amount equivalent to the additional income-tax calculated under sub-clause (A) or sub-clause (B), as the case may be . . .

(2) Where a return has been made under section 139, or in response to a notice under sub-section (1) of section 142, the Assessing Officer shall, if he considers it necessary or expedient to ensure that the assessee has not understated the income or has not computed excessive loss or has not underpaid the tax in any manner, serve on the assessee a notice requiring him, on a date to be specified therein, either to attend his office or to produce, or cause to be produced there, any evidence on which the assessee may rely in support of the return :

Provided that no notice under this sub-section shall be served on the assessee after the expiry of twelve months from the end of the month in which the return is furnished.

(3) On the day specified in the notice issued under sub-section (2) or as soon afterwards as may be, after hearing, such evidence as the assessee may produce and such other evidence as the Assessing Officer may require on specified points, and after taking into account all relevant material which he has gathered, the Assessing Officer shall, by an order in writing, make an assessment of the total income or loss of the assessee, and determine the sum payable by him on the basis of such assessment.

(4) Where a regular assessment under sub-section (3) of this section or section 144 is made—

(a) any tax or interest paid by the assessee under sub-section (1) shall be deemed to have been paid towards such regular assessment ;

(b) if no refund is due on regular assessment or the amount refunded under sub-section (1) exceeds the amount refundable on regular assessment, the whole or the excess amount so refunded shall be deemed to be tax payable by the assessee and the provisions of this Act shall apply accordingly . . ."

8.1.2 Thereafter, the issue was considered thus[1] :

"It is thus clear that the Assessing Officer even after issuing intimation after making adjustments as per provisions of section 143(1) of the Act can call upon the assessee, if he considers it necessary or expedient to ensure that the assessee has not understated the income or has not computed excessive loss or has not underpaid the tax in any manner. Once this opinion is formed then the Assessing Officer will have to serve on the assessee a notice under section 143(2) of the Act requiring him to produce evidence before him on the date specified in the notice. This is permissible in view of saving clause in section 143(1) of the Act. Section 143(1) of the Act is to be exercised without prejudice to the provisions of sub-section (2) of section 143 of the Act. However, exercise of powers under section 143(1) is not made permissible after issuance of notice under section 143(2) of the Act. The Assessing Officer cannot exercise powers under section 143(1) of the Act as he himself has decided to make regular assessment under section 143(3) of the Act. That in section 143(2) like under section 143(1) powers are not saved. As the Assessing Officer has called upon the assessee to furnish evidence to satisfy himself about the correctness or legality of the claim made by the assessee in his return, hence, only after hearing the assessee and after considering the evidence that may be produced by the assessee the Assessing Officer has to make the order in writing making assessment of the total income or loss of the assessee and he has to determine the amount payable on the basis of such assessment, that is, under section 143(3) of the Act. Mr. Shelat, learned counsel for the Revenue, fairly stated that notice under section 143(2) of the Act cannot be withdrawn. Notice under section 143(2) of the Act is a step towards regular assessment under section 143(3) of the Act and, therefore, in the absence of any provision it is not open to make assessment in any other manner than provided as per section 143(3) of the Act. . . .

Powers to make assessment in terms of its proviso can be invoked and when the claim is prima facie inadmissible or prima facie admissible, as the case may be, adjustment is to be made. The word prima

1. Page 146 of 222 ITR.

facie clearly indicates that it must be first evidenced. A decision on the debatable issue is not envisaged. Issuance of notice under section 143(2) of the Act suggests that the Assessing Officer has determined to make assessment under section 143(3) of the Act. It is clear, looking to the language used in different sub-sections that an order under section 143(1) is a summary one and the Assessing Officer on perusal of the return, that is, computation of income, is able to accept it as it is or with necessary adjustments as indicated in sub-clause (a) of sub-section (1) of section 143 of the Act. The submission made by learned counsel for the Revenue is that even after issuance of notice under section 143(2) of the Act, it is permissible for the Assessing Officer to assess under section 143(1) of the Act. One has to examine the claim on account of results of adjustments made in the income shown in the return whether it results in increase or loss declared in the return is reduced or is converted into income. If that is so it would entail further tax at the rate of 20 per cent. on the income so increased or a further tax of 20 per cent. on the loss so reduced as if it is income and the assessee will be charged as per sub-section (1A) of section 143 of the Act. With a view to see that taxpayers in the return furnish details with accuracy and correctness this provision is made. The assessee is aware about the provision and should take care that no incorrect statement is made with a view to save additional tax which may be imposed on him. However, when the Assessing Officer is not assessing the correctness about the claim which is either prima facie admissible or prima facie inadmissible, and the Assessing Officer with a view to ensure that the assessee has not computed excessive loss or has not underpaid tax in any manner has issued notice under section 143(2) of the Act, then there should be evidence before him and on the basis of the evidence that may be produced by the assessee, assessment is to be made under section 143(3) of the Act, and the assessee will be liable to tax in the manner laid down in the Act if he is required to pay. After calling upon the assessee to produce evidence if the Assessing Officer is sending intimation instead of making regular assessment under section 143(3) of the Act then in that case the Assessing Officer would assess and would charge tax as per section 143(1A) of the Act which is not contemplated under section 143(3) of the Act and thus what is not permissible under section 143(3) of the Act cannot be made permissible by allowing the Assessing Officer to resort to section 143(1) of the Act . . .

In this view of the matter, we are of the opinion that after issuance of notice under section 143(2) of the Act, it is not open to the Assessing Officer to make adjustment or to pass an order under section 143(1) of the Act but he has to make assessment in accordance with law, i.e., under section 143(3) of the Act."

**9** These decisions were rendered in the context of the provisions then in existence which had following notable features :

(a) sub-section (1A) in terms of which, if any adjustments had resulted in increased total income, an additional income-tax at the rate of 20 per cent. on the difference would be levied.

(b) the intimation to be sent under sub-section (1) was expressly stated to be "without prejudice to the provision of sub-section (2)".

None the less, the basic distinction that was noted was : the procedure under sub-section (1) was summary in nature whereas that under sub-section (2) was a regular assessment.

**10** Section 143 of the Act has since then undergone considerable change. Sub-section (1) stands modified and now specifies with clarity the nature of adjustments. Sub-section (1A) contemplates processing of returns through Centralized Processing. Since we are principally concerned in the present matter with the effect and applicability of subsection (1D), the legislative history relating to said sub-section (1D) is dealt with in detail hereunder :

(A) Sub-section (1D) was inserted vide the Finance Act, 2012 as under :

"(1D) Notwithstanding anything contained in subsection (1), the processing of a return shall not be necessary, where a notice has been issued to the assessee under sub-section (2)."

The explanatory note to the Finance Act, 2012 relevant to the proposed insertion of sub-section (1D) was :

"Under the existing provisions, every return of income is to be processed under sub-section (1) of section 143 and refund, if any, due is to be issued to the taxpayer. Some returns of income are also selected for scrutiny which may lead to raising a demand for taxes although refunds may have been issued earlier at the time of processing.

It is therefore proposed to amend the provisions of the Income-tax Act to provide that processing of return will not be necessary in a case where notice under sub-section (2) of section 143 has been issued for scrutiny of the return."

(B) The Finance Act, 2016[1] contemplated substitution of sub-section (1D) and insertion of a proviso with effect from April 1, 2017 as follows :

1. [2016] 384 ITR (St.) 1.

"(1D) Notwithstanding anything contained in sub-section (1), the processing of a return shall not be necessary before the expiry of the period specified in the second proviso to sub-section (1), where a notice has been issued to the assessee under sub-section (2) :

Provided that such return shall be processed before the issuance of an order under sub-section (3)."

The relevant explanatory Note to Finance Act, 2016 was :

"56. Processing under section 143(1) of the Income-tax Act be mandated before assessment :

56.1 Under the existing provision of sub-section (1D) of section 143 of the Income-tax Act, processing of a return is not necessary where a notice has been issued to the assessee under sub-section (2) of the said section.

56.2 The said sub-section (1D) of the aforesaid section has been amended to provide that in cases where a notice has been issued under sub-section (2) of section 143 of the Income-tax Act the processing of return shall not be necessary before the expiry of one year from the end of the financial year in which the return is furnished. However, it is mandated to process the return before the issuance of order under sub-section (3) of section 143 of the Income-tax Act.

56.3 *Applicability* : This amendment takes effect from the 1st of April, 2017 and will, accordingly apply in relation to the assessment year 2017-18 and subsequent years."

(C) The aforementioned substitution of sub-section (1D), however, never came into effect, as by the Finance Act, 2017[1] the said sub-section in the earlier form was retained and the text of the proviso was also modified. Effectively, on and with effect from April 1, 2017, sub-section (1D) and the proviso are :

"(1D) Notwithstanding anything contained in subsection (1), the processing of a return shall not be necessary, where a notice has been issued to the assessee under sub-section (2) :

Provided that the provisions of this sub-section shall not apply to any return furnished for the assessment year commencing on or after the 1st day of April, 2017."

The concerned explanatory note to the Finance Act, 2017 was :

"59. Processing of return within the prescribed time and enable withholding of refund in certain cases.

1. [2017] 393 ITR (St.) 1.

59.1 Before amendment by the Finance Act, 2016, the provisions of sub-section (1D) of section 143 of the Income-tax Act specify that the processing of a return shall not be necessary, where a notice has been issued to the assessee under sub-section (2) of the said section.

59.2 The said sub-section was amended vide Finance Act, 2016 and it was provided that with effect from the assessment year 2017-18, processing under section 143(1) of the Income-tax Act is to be done before passing of assessment order.

59.3 In order to address the grievance of delay in issuance of refund in genuine cases, a proviso has been inserted in section 143(1D) of the Income-tax Act specifying that the provisions of the said sub-section shall cease to apply in respect of returns furnished for the assessment year 2017-18 and onwards.

59.4 However, to address the concern of recovery of revenue in doubtful cases, a new section 241A has been inserted in the Income-tax Act to provide that, for the returns furnished for the assessment year commencing on or after April 1, 2017, where refund of any amount becomes due to the assessee under section 143(1) of the Income-tax Act and the Assessing Officer is of the opinion that grant of refund may adversely affect the recovery of revenue, he may, for the reasons recorded in writing and with the previous approval of the Principal Commissioner or Commissioner, withhold the refund up to the date on which the assessment is made.

59.5 *Applicability* : These amendments take effect from April 1, 2017 and accordingly apply to returns furnished for the assessment year 2017-18 and subsequent years."

(D) The Finance Act, 2017[1] also inserted section 241A in the Act as under :

"241A. *Withholding of refund in certain cases*.—For every assessment year commencing on or after the 1st day of April, 2017 where refund of any amount becomes due to the assessee under the provisions of sub-section (1) of section 143 and the Assessing Officer is of the opinion, having regard to the fact that a notice has been issued under sub-section (2) of section 143 in respect of such return, that the grant of the refund is likely to adversely affect the revenue, he may, for reasons to be recorded in writing and with the previous approval of the Principal Commissioner or Commissioner, as the case may be, withhold the refund up to the date on which the assessment is made."

1. [2017] 393 ITR (St.) 1.

Consequently, the relevant parts of sub-sections (1) to (3) of section 143 of the Act, as they stand today are as under : **11**

"143. *Assessment*.—(1) Where a return has been made under section 139, or in response to a notice under sub-section (1) of section 142, such return shall be processed in the following manner, namely :

(a) the total income or loss shall be computed after making the following adjustments, namely :

(i) any arithmetical error in the return ;

(ii) an incorrect claim, if such incorrect claim is apparent from any information in the return ;

(iii) disallowance of loss claimed, if return of the previous year for which set off of loss is claimed was furnished beyond the due date specified under sub-section (1) of section 139 ;

(iv) disallowance of expenditure indicated in the audit report but not taken into account in computing the total income in the return ;

(v) disallowance of deduction claimed under sections 10AA, 80-IA, 80-IAB, 80-IB, 80-IC, 80-ID or section 80-IE, if the return is furnished beyond the due date specified under sub-section (1) of section 139 ; or

(vi) addition of income appearing in Form 26AS or Form 16A or Form 16 which has not been included in computing the total income in the return :

Provided that no such adjustments shall be made unless an intimation is given to the assessee of such adjustments either in writing or in electronic mode :

Provided further that the response received from the assessee, if any, shall be considered before making any adjustment, and in a case where no response is received within thirty days of the issue of such intimation, such adjustments shall be made :

Provided also that no adjustment shall be made under sub-clause (vi) in relation to a return furnished for the assessment year commencing on or after the 1st day of April, 2018 ;

(b) the tax, interest and fee, if any, shall be computed on the basis of the total income computed under clause (a) ;

(c) the sum payable by, or the amount of refund due to, the assessee shall be determined after adjustment of the tax, interest and fee, if any, computed under clause (b) by any tax deducted at source, any tax collected at source, any advance tax paid, any relief allowable under section 89, any relief allowable under an agreement under section 90

or section 90A, or any relief allowable under section 91, any rebate allowable under Part A of Chapter VIII, any tax paid on self-assessment and any amount paid otherwise by way of tax, interest or fee ;

(d) an intimation shall be prepared or generated and sent to the assessee specifying the sum determined to be payable by, or the amount of refund due to, the assessee under clause (c) ; and

(e) the amount of refund due to the assessee in pursuance of the determination under clause (c) shall be granted to the assessee :

Provided that an intimation shall also be sent to the assessee in a case where the loss declared in the return by the assessee is adjusted but no tax, interest or fee is payable by, or no refund is due to him :

Provided further that no intimation under this sub-section shall be sent after the expiry of one year from the end of the financial year in which the return is made.

*Explanation.*—For the purposes of this sub-section,—

(a) 'an incorrect claim apparent from any information in the return' shall mean a claim, on the basis of an entry, in the return,—

(i) of an item, which is inconsistent with another entry of the same or some other item in such return ;

(ii) in respect of which the information required to be furnished under this Act to substantiate such entry has not been so furnished ; or

(iii) in respect of a deduction, where such deduction exceeds specified statutory limit which may have been expressed as monetary amount or percentage or ratio or fraction ;

(b) the acknowledgment of the return shall be deemed to be the intimation in a case where no sum is payable by, or refundable to, the assessee under clause (c), and where no adjustment has been made under clause (a).

(1A) For the purposes of processing of returns under sub-section (1), the Board may make a scheme for centralized processing of returns with a view to expeditiously determining the tax payable by, or the refund due to, the assessee as required under the said sub-section.

(1B) Save as otherwise expressly provided, for the purpose of giving effect to the scheme made under sub-section (1A), the Central Government may, by notification in the Official Gazette, direct that any of the provisions of this Act relating to processing of returns shall not apply or shall apply with such exceptions, modifications and

adaptations as may be specified in that notification ; so, however, that no direction shall be issued after the 31st day of March, 2012.

(1C) Every notification issued under sub-section (1B), along with the scheme made under sub-section (1A), shall, as soon as may be after the notification is issued, be laid before each House of Parliament.

(1D) Notwithstanding anything contained in sub-section (1), the processing of a return shall not be necessary, where a notice has been issued to the assessee under sub-section (2) :

Provided that the provisions of this sub-section shall not apply to any return furnished for the assessment year commencing on or after the 1st day of April, 2017.

(2) Where a return has been furnished under section 139, or in response to a notice under sub-section (1) of section 142, the Assessing Officer or the prescribed income-tax authority, as the case may be, if, considers it necessary or expedient to ensure that the assessee has not understated the income or has not computed excessive loss or has not under-paid the tax in any manner, shall serve on the assessee a notice requiring him, on a date to be specified therein, either to attend the office of the Assessing Officer or to produce, or cause to be produced before the Assessing Officer any evidence on which the assessee may rely in support of the return :

Provided that no notice under this sub-section shall be served on the assessee after the expiry of six months from the end of the financial year in which the return is furnished.

(3) On the day specified in the notice issued under sub-section (2), or as soon afterwards as may be, after hearing such evidence as the assessee may produce and such other evidence as the Assessing Officer may require on specified points, and after taking into account all relevant material which he has gathered, the Assessing Officer shall, by an order in writing, make an assessment of the total income or loss of the assessee, and determine the sum payable by him or refund of any amount due to him on the basis of such assessment . . ."

**12** Clause (a) of sub-section (1) of section 143 has six sub-clauses specifying the kinds of adjustments which are required to be made for computing the total income or loss. Such adjustments are in the nature of "arithmetical error in the return" ; incorrect claim "apparent from any information in the return" ; disallowance of loss if the return of the previous year with respect

to which such loss is claimed was furnished "beyond the due date" ; disallowance of expenditure indicated in the audit report if it has "not taken into account in computing the total income" ; disallowance of deductions specified in sub-clause if the "return is furnished beyond the due date" ; and addition of income as specified in sub-clause (vi) if it was not "included in computing the total income". All these features deal with matters which are apparent from the return and the inconsistency is evident on the face of it. Upon causing such adjustments after due intimation or notice to the assessee, the element of tax, interest and fee is to be computed in terms of clause (b). Thereafter, in terms of clause (c), due credit to the amount of tax paid and any relief that is allowable is to be given and the net amount payable or to be refunded, is to be computed. The intimation to be generated under clause (d) is on the basis of such exercise and if any refund is due, the same has to be granted in terms of clause (e). Thus, at every stage in sub-section (1) the return submitted by the assessee forms the foundation, with respect to which, if any of the inconsistencies referred to in various sub-clauses of clause (a) are found, appropriate adjustments are to be made.

On the other hand, the exercise of power under sub-section (2) of section 143 of the Act, leading to the passing of an order under sub-section (3) thereof, is to be undertaken, where it is considered necessary or expedient to ensure that the assessee :

- has not understated the income, or
- has not computed excessive loss, or
- has not under-paid the tax in any manner.

The issuance of notice and consequent proceedings are premised on any of the aforesaid three postulates. In other words, the return filed by the assessee itself calls for or requires a further probe and deeper consideration. The guiding principle is to ensure that the income is not understated or the loss is not overstated, or the tax is not under-paid in any manner. Upon issuance of notice, the assessee is entitled to produce evidence in support of his case. After hearing the assessee and considering the evidence so produced, by an order in writing, the assessment of total income or loss is to be made.

**13** The nature of exercise of power under sub-section (1) as against that under sub-sections (2) and (3) is thus completely different. In the former case, the matter is processed, only to check whether any apparent inconsistencies are evident on the face of the return and connected material which may call for any adjustment while in the latter case, the matter is scrutinized after taking into account such evidence as the assessee may

produce. The exercise in the latter case is to ensure that there is no understating of income or overstating of loss or under-payment of the tax in any manner. In other words, the veracity of the return is checked threadbare rather than considering mere apparent inconsistencies from the return. Thus, the nature of power under these two provisions, as found by this court in *CIT* v. *Gujarat Electricity Board* continues to bear the same distinction.

The power under sub-section (1) of section 143 of the Act is summary in nature designed to cause adjustments which are apparent from the return while that under sub-sections (2) and (3) is to scrutinize the return and cause deeper probe to arrive at the correct determination of the liability of the assessee.

14 The exercise of power under sub-sections (2) and (3) of section 143 of the Act is thus premised on non-acceptance of what is evident from the return itself and to ensure that there is no avoidance of tax in any manner. The dimension of such power is far greater and deeper than mere adjustments to be made in respect of what is available from the return. Once such scrutiny is undertaken and proceedings are initiated by issuance of a notice under sub-section (2) of section 143, it would be anomalous and incongruent that while such proceedings so initiated are pending, the return be processed under sub-section (1) of section 143, which may in a given case, entail payment of refund. Logically, the outcome of the exercise initiated through notice under sub-section (2) of section 143, must determine whether any refund is due and payable. If the return itself is under probe and scrutiny, such return cannot be the foundation to sustain a claim for refund till such scrutiny is not complete. Considering the nature of power exercisable under these two limbs of section 143, the inescapable conclusion is that the processing of return under sub-section (1) of section 143 must await the further exercise of power of scrutiny assessment under sub-sections (2) and (3) of section 143. If the power under sub-section (2) of section 143 of the Act is initiated in a manner known to law, there cannot be any insistence that the processing under sub-section (1) of section 143 be completed and refund be made before the scrutiny pursuant to notice under sub-section (2) of section 143 is over.

15 The afore-stated conclusion is fortified and strengthened by clear stipulation to that effect in sub-section (1D) of section 143. Irrespective of some change in the text of the said provision which was sought to be introduced by the Finance Act, 2016 and not accepted by Finance Act, 2017, the legislative intent is clear from the expression, ". . . the processing of a return shall not be necessary, where a notice has been issued to the assessee

under sub-section (2)" and by use of non obstante clause. Though the period for which it would not be necessary to process the return was sought to be specified by Finance Act, 2016, mere absence of such period in the provision as it stands today, makes no difference. The above quoted portion from the provision and use of non obstante clause indicate with sufficient clarity the intent of Parliament that in cases where notice under sub-section (2) is issued and proceedings are initiated, the processing of a return under sub-section (1) shall not be necessary.

**16** The expression "shall not be necessary" is used in various statutes and even in the Constitution of India. This expression is used in the first proviso to article 311(2) and in proviso to article 320(3) of the Constitution of India. Some of the cases in which similar expression occurring in statutes was taken into account and effect was given to its plain language are :

(i) Proviso to section 63(3) of the Motor Vehicles Act, 1939—in *Mohd. Ibrahim* v. *State Transport Appellate Tribunal*.[1]

(ii) Order XXX, rule 4 of the Code of Civil Procedure—in *Sohanlal* v. *Amir Chand and Sons*[2], *Upper India Cable Co.* v. *Bal Kishan*[3] and in *Brij Kishore Sharma* v. *Ram Singh and Sons*[4].

(iii) Proviso to section 68 of the Indian Evidence Act, 1872—in *Rasammal Issetheerammal Fernandez etc.* v. *Joosa Mariyam Fernandez*[5] .

As against the general principle which mandates an action in a particular manner, when an exception is to be carved out, the relevant provisions stipulate "it shall not be necessary" to adhere to and follow the manner mandated by such general principle ; and if the contingency contemplated by such exception arises, the general principle is to stand overridden.

**17** The intent to have the general principle emanating from sub-section (1) of section 143 overridden, in case where the proceedings are initiated pursuant to notice under sub-section (2) of the Act, gets more pronounced and emphasized by use of non obstante clause in sub-section (1D). Recently, while dealing with the non obstante clause in section 26(1) of the Provincial Small Cause Courts Act, 1887 this court observed in *Vaishali Abhimanyu Joshi* v. *Nanasaheb Gopal Joshi*[6] as under :

> "33. 'Notwithstanding anything contained elsewhere in this Act' as used in section 26(1) of the 1887 Act are words of expression of the

1. [1970] 2 SCC 233.
2. [1973] 2 SCC 608.
3. [1984] 3 SCC 462.
4. [1996] 11 SCC 480.
5. [2000] 7 SCC 189.
6. [2017] 14 SCC 373.

widest amplitude engulfing the contrary provisions contained in the Act. The suit in question has been filed by the plaintiff for enforcement of his right as a licensor after allegedly terminating the gratuitous licence of the appellant. On a plain reading, Item 11 of Schedule II covers determination or enforcement of any such right or interest in immovable property. But by virtue of section 26, sub-section (1) as applicable in the State of Maharashtra, Item 11 of Schedule II has to give way to section 26(1) and a suit between licensor and licensee which is virtually a suit for recovery of immovable property is fully maintainable in Judge, Small Cause Court that is why the suit has been instituted by the plaintiff in the Judge, Small Cause Court claiming the right and interest in the immovable property.

35. A statutory provision containing non obstante clause has to be given full effect. This court in *Union of India* v. *G. M. Kokil*[1] has laid down in para 11 as below : (SCC page 203)

'11 . . . It is well known that a non obstante clause is a legislative device which is usually employed to give overriding effect to certain provisions over some contrary provisions that may be found either in the same enactment or some other enactment, that is to say, to avoid the operation and effect of all contrary provisions. Thus the non obstante clause in section 70, namely, "notwithstanding anything contained in that Act" must mean notwithstanding anything to the contrary contained in that Act and as such it must refer to the exempting provisions which would be contrary to the general applicability of the Act'."

**18** In the premises, we hold that in respect of the assessment years ending on March 31, 2017 or before, if a notice was issued in conformity with the requirements stated in sub-section (2) of section 143 of the Act, it shall not be necessary to process the refund under sub-section (1) of section 143 of the Act and that the requirement to process the return shall stand overridden.

**19** We must now deal with the issue whether any intimation is required to be given to the assessee that because of initiation of proceedings pursuant to notice under sub-section (2) of section 143 of the Act processing of return in terms of sub-section (1) of section 143 of the Act, would stand deferred. The processing of return in terms of sub-section (1A) of section 143 of the Act is to be done through centralized processing and as stated earlier, the scope of processing under sub-section (1) of section 143 of the

1. [1984] Supp. SCC 196.

Act is purely summary in character. Once deeper scrutiny is undertaken and the matter is being considered from the perspective whether there is any avoidance of tax in any manner, issuance of notice under sub-section (2) itself is sufficient indication. Sub-section (1D) of section 143 of the Act does not contemplate either issuance of any such intimation or further application of mind that the processing must be kept in abeyance. It would not, therefore, be proper to read into said provision the requirement to send a separate intimation. In our view, issuance of notice under sub-section (2) of section 143 is enough to trigger the required consequence. Any other intimation is neither contemplated by the statute nor would it achieve any purpose.

**20** Consequently, the submission that the intimation dated July 23, 2018 must be held to be invalid, inter alia on the ground that it was issued well after the period within which the return was required to be processed under sub-section (1) of section 143 of the Act, must be rejected.

**21** However, in so far as returns filed in respect of the assessment year commencing on or after April 1, 2017, a different regime has been contemplated by Parliament. Section 241A of the Act requires a separate recording of satisfaction on the part of the Assessing Officer that having regard to the fact that a notice has been issued under sub-section (2) of section 143, the grant of refund is likely to adversely affect the revenue ; whereafter, with the previous approval of the Principal Commissioner or Commissioner and for reasons to be recorded in writing, the refund can be withheld.

Since the statute now envisages exercise of power of withholding of refund in a particular manner, it goes without saying that for the assessment year commencing after April 1, 2017 the requirements of section 241A of the Act must be satisfied.

**22** We will, therefore, have to see whether in so far as the assessment year 2017-18 is concerned, the order dated March 14, 2019 satisfies the required statutory parameters or not.

In terms of second proviso to sub-section (1) of section 143 of the Act, the required intimation under said sub-section must be given before the expiry of one year from the end of the financial year in which the return is made. In respect of the assessment year 2017-18, the return having been filed on November 25, 2017, period available in terms of said second proviso was up to March 31, 2019, without taking into account the fact that revised return was filed on July 13, 2018.

In the present case, the exercise of power on March 14, 2019 was not only after issuance of notice under sub-section (2) of section 143 and after

recording due satisfaction in terms of section 241A of the Act, but was also well within the period contemplated by sub-section (1) of section 143 of the Act for causing due intimation.

Whether the satisfaction recorded in terms of the said section 241A of the Act was otherwise correct or not and whether a case for withholding of refund was made out or not, are not the issues that arise for our consideration. For the present purposes, whether exercise of power is facially in conformity with the statutory provisions is the issue and we are satisfied that there is nothing in the exercise of power that led to the passing of the order dated March 14, 2019 which could be said to have violated any statutory requirements.

In so far as the assessment year 2014-15 is concerned, final assessment **23**
order passed under section 143(3) of the Act indicates that the appellant is entitled to refund of Rs. 733 crores ; while for the assessment year 2015-16 there is a demand of Rs. 582 crores. During the course of hearing, it was suggested on behalf of the respondents that demands in respect of earlier assessment years including the liability as a result of the order dated December 28, 2019 as referred to in para 5.1 hereinabove being outstanding, the respondents would be entitled to invoke the requisite power under section 245 of the Act to set off the amount of refund payable in respect of the assessment year 2014-15 against tax remaining payable.

Since the requisite action is not even initiated, we say nothing in that respect. In the premises, we direct that the amount of Rs. 733 crores shall be refunded to the appellant within four weeks from today subject to any proceedings that the Revenue may deem appropriate to initiate in accordance with law. We also direct the respondents to conclude the proceedings initiated pursuant to notice under sub-section (2) of section 143 of the Act in respect of the assessment years 2016-17 and 2017-18 as early as possible.

Except for the directions as indicated above, we see no merit in any of **24**
the contentions advanced by the appellant. This appeal is, therefore, dismissed without any order as to costs.

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**[2020] 424 ITR 704 (SC)**

[IN THE SUPREME COURT OF INDIA]

# RAJASTHAN STATE ELECTRICITY BOARD

*v.*

# DEPUTY COMMISSIONER OF INCOME-TAX (ASSESSMENT) AND ANOTHER

ASHOK BHUSHAN and MOHAN M. SHANTANAGOUDAR JJ.

March 19, 2020.

**SS ▸ ITA 1961, ss 32(2), 143(1A)**
**AY ▸ 1991-92**
**HF ▸ Assessee**

ASSESSMENT—ADDITIONAL TAX—CHANGE OF LAW—AMENDMENT TO EFFECT THAT WHERE LOSS DECLARED BY ASSESSEE REDUCED BY REASON OF PRIMA FACIE ADJUSTMENTS, ADDITIONAL TAX LEVIABLE—ONLY TO BE INVOKED WHERE LOWER AMOUNT SHOWN IN RETURN BY ASSESSEE WAS WITH INTENT TO EVADE TAX—ASSESSEE BY BONA FIDE OVERSIGHT CLAIMING DEPRECIATION AT 100 PER CENT. INSTEAD OF AT 75 PER CENT.—RETURN REMAINING ONE OF LOSS—NO INTENTION TO EVADE TAX—MECHANICAL LEVY OF ADDITIONAL TAX UNCALLED FOR—INCOME-TAX ACT, 1961, SS. 32(2), 143(1A).

INTERPRETATION OF TAXING STATUTES—CONSEQUENCES AND HARDSHIP NOT RELEVANT—PURPOSE AND OBJECT OF STATUTE TO BE SEEN.

*The object of section 143(1A) of the Income-tax Act, 1961 as substituted by the Finance Act, 1993 with effect from April 1, 1989 was the prevention of evasion of tax. The Memorandum Explaining the Provisions of the Finance Bill* ([1993] 200 ITR (St.) 140) *was also to persuade assessees to file their income-tax returns carefully to avoid mistakes. The provisions of section 143(1A) should be made to apply only to tax evaders. Section 143(1A) can only be invoked where it is found on the facts that the lower amount stated in the return filed by the assessee is a result of an attempt to evade tax lawfully by the assessee.*

*Although while interpreting a tax legislation the consequences and hardship are not looked into, the purpose and object by which taxing statutes have been enacted cannot be lost sight of.*

*For the assessment year 1991-92, the assessee, in its return filed on December 31, 1991, showed a loss of Rs. 427,39,32,972. Due to a bona fide mistake the assessee claimed depreciation at 100 per cent. on the written down value of assets instead of at 75 per cent. An intimation under section*

*143(1)(a) of the Income-tax Act, 1961 was issued by the Assessing Officer disallowing 25 per cent. of the depreciation, restricting the depreciation to 75 per cent. and levying additional tax under section 143(1A) of the Act of Rs. 8,63,64,827. The assessee filed an application for rectification of the demand and a petition to the Commissioner for revision stating that even after allowing only 75 per cent. of depreciation the income of the assessee remained a loss at Rs. 3,43,94,90,393 and prayed for quashing the demand of additional tax. The application for rectification was rejected by the Assessing Officer as was the revision petition by the Commissioner. The assessee filed a writ petition which a single judge allowed quashing the levy of additional tax under section 143(1A). The Department filed an appeal which the Division Bench allowed upholding the demand of additional tax. On appeal :*

Held, *allowing the appeal, that by the Taxation Laws (Amendment) Act, 1991, the third proviso was inserted in section 32 to provide that from the assessment year 1991-92 the depreciation shall be restricted to seventy-five per cent. on the written down value. The return was filed by the assessee on December 31, 1991, prior to which date the Taxation Laws (Amendment) Act, 1991 had come into operation. It was due to a bona fide mistake and oversight that the assessee claimed 100 per cent. depreciation instead of 75 per cent. Even after reduction of 25 per cent. depreciation the return was one of loss. In claiming 100 per cent. depreciation the assessee claimed that there was no intention to evade tax and the claim was only a bona fide mistake. The object of section 143(1A) was the prevention of evasion of tax. The Memorandum Explaining the Provisions of the Finance Bill stated that the object was to persuade assessees to file income-tax returns carefully to avoid mistakes. The Commissioner in deciding the revision petition had not made any observation that the claim to 100 per cent. depreciation was with intent to evade payment of tax lawfully payable by the assessee. The mechanical application of section 143(1A) in the facts of the present case was uncalled for.*

*Decision of the Jaipur Bench of the Rajasthan High Court in* DY. CIT (ASSTT.) *v.* RAJASTHAN STATE ELECTRICITY BOARD [2008] 299 ITR 253 (Raj) *reversed.*

CIT *v.* SATI OIL UDYOG LTD. [2015] 372 ITR 746 (SC) *applied*.

Cases referred to :

CIT (Deputy) (Asstt.) *v.* Ashok Paper Mills Ltd. [2002] 256 ITR 673 (Gauhati) (para 17)

CIT (Deputy) (Asstt.) *v.* Rajasthan State Electricity Board [2008] 299 ITR 253 (Raj) (para 1)

CIT *v.* Sati Oil Udyog Ltd. [2015] 372 ITR 746 (SC) (paras 17, 22)

J. K. Synthetics Ltd. *v.* Asst. CIT [2001] 251 ITR 200 (SC) (para 18)

Rajasthan State Electricity Board *v.* Deputy CIT (Asstt.) [1993] 200 ITR 434 (Raj) (para 4)

Sati Oil Udyog Ltd. *v.* CIT [1998] 232 ITR 502 (Gauhati) (para 17)

Varghese (K. P.) *v.* ITO [1981] 131 ITR 597 (SC) (para 18)

**Civil Appeal No. 8590 of 2010.**

Appeal from the judgment and order dated November 13, 2007 of the Jaipur Bench of the Rajasthan High Court in D. B. Civil Special Appeal (Writ) No. 837 of 1993. The judgment of the High Court is reported as *Deputy CIT (Asstt.)* v. *Rajasthan State Electricity Board* [2008] 299 ITR 253 (Raj).

*Arijit Prasad*, Senior Advocate, (*Rohit K. Singh*, *Mirza Kayesh Begg* and *Ms. Anshruta Maheshwari*, Advocates, with him) for the appellant.

*Rupesh Kumar*, *Mrs. Gargi Khanna*, *Shreyash Bhardwaj* and *Mrs. Anil Katiyar*, Advocates, for the respondents.

**JUDGMENT**

The judgment of the court was delivered by

1 ASHOK BHUSHAN J.—This appeal has been filed by the assessee challenging the Division Bench judgment dated November 13, 2007 of the High Court of Judicature for Rajasthan at Jaipur Bench, Jaipur by which D. B. Civil Special Appeal (Writ) No. 837 of 1993[1] filed by the Revenue has been allowed upholding the demand of additional tax under section 143(1A) of the Income-tax Act, 1961.

2 Brief facts necessary to be noted for deciding this appeal are :

The assessee is a Government company as defined under section 617 of the Companies Act, 1956. The assessee filed return on December 30, 1991 for the assessment year 1991-92 showing a loss amounting to Rs. (-) 427,39,32,972. Due to a bona fide mistake the assessee claimed 100 per cent. depreciation of Rs. 333,77,70,317 on the written down value of assets instead of 75 per cent. depreciation. Under the unamended section 32(2) of the Income-tax Act, 1961, the assessee was entitled to claim 100 per cent. depreciation. However, after the amendment the depreciation could only be 75 per cent. The assessee supported the returns with provisional revenue account, balance-sheet as on March 31, 1991, details of gross fixed assets, computation chart and depreciation chart. No tax was payable on the said return by the assessee. No notice under section 143(2) of the Income-tax Act, 1961 was received by the assessee.

1. *Deputy CIT (Asstt.)* v. *Rajasthan State Electricity Board* [2008] 299 ITR 253 (Raj).

3 An intimation under section 143(1)(a) of the Income-tax Act, 1961 dated February 12, 1992 was issued by the Assessing Officer disallowing 25 per cent. of the depreciation, restricting the depreciation to 75 per cent. Additional tax under section 143(1A) of the Income-tax Act, 1961 amounting to Rs. 8,63,64,827 was demanded. The assessee filed an application under section 154 of the Income-tax Act, 1961 dated February 18, 1992 praying for rectification of the demand. The assessee also filed a petition under section 264 of the Income-tax Act, 1961 against the demand of additional tax. In the petition it was stated that even after allowing only 75 per cent. of depreciation the income of the assessee remained to be in loss to Rs. 3,43,94,90,393. The assessee prayed for quashing the demand of additional tax. The application filed under section 154 of the Income-tax Act, 1961 was rejected by the Assessing Officer on February 28, 1992. The revision petition under section 264 of the Income-tax Act, 1961 came to be dismissed by the Commissioner of Income-tax by order dated March 31, 1992. The Commissioner of Income-tax rejected the revision petition by giving the following reasoning :

> "A plain reading of the provisions of section 143(1A) shows that whenever adjustment is made, additional tax has to be charged at 20 per cent. of the tax payable on such 'excess amount'. The 'excess amount' refers to the increase in the income and by implication the reduction in loss where even after the addition there is negative income. The *Explanation* to section 143(1A)(b) provides that the tax payable on such excess means the tax that would have been chargeable on the amount of adjustment to the total income. Where the adjustment exceeds the income determined. Clearly, therefore, in this case the additional tax had to be charged on the basis of the tax chargeable on the sum of Rs. 83,44,42,579 added by the Assessing Officer."

4 Aggrieved by the order of the Commissioner of Income-tax challenging the demand of additional tax which was reduced to an amount of Rs. 7,67,68,717, Writ Petition No. 2267 of 1992 was filed by the assessee in the High Court of Judicature for Rajasthan, Bench at Jaipur. The learned single judge vide judgment dated January 19, 1993[1] allowed the writ petition quashing the levy of additional tax under section 143(1A). The Revenue aggrieved by the judgment of the learned single judge filed a special appeal which has been allowed by the Division Bench of the High Court vide its judgment dated November 13, 2007 upholding the demand of additional tax. The assessee aggrieved by the judgment of the Division Bench has come up in this appeal.

1. *Rajasthan State Electricity Board* v. *Deputy CIT (Asstt.)* [1993] 200 ITR 434 (Raj).

5 We have heard Shri Arijit Prasad, learned senior counsel appearing for the appellant and Shri Rupesh Kumar, learned counsel for the respondents.

6 Shri Arijit Prasad referring to Circular No. 549, dated October 31, 1989[1] of Central Board of Direct Taxes submits that 20 per cent. additional tax sought to be imposed under section 143(1A) of the 1961 Act is in the nature of penalty and can be levied only when the assessee had intentionally sought to file an incorrect return. It is submitted that such additional tax could only become payable in case where assessee was assessed to an income for the purpose of tax and could not apply where there was no income or there was loss. The intent of the Legislature in enacting provision of section 143(1A) was to ensure that the assessee also declares his loss in the return correctly and where the assessee deliberately or intentionally filed false returns, he was liable to pay additional income-tax. It is submitted that unabsorbed losses and unabsorbed depreciation were to be carried forward to future years to be set off against profits and it did not in any manner affect business loss. He submits that business loss suffered by the assessee had not reduced because of the bona fide mistake committed by the appellant in calculating the depreciation. The assessee was in loss and continued to be in loss. Reduction in depreciation from 100 per cent. to 75 per cent. did not amount to reduction in loss and additional tax under section 143(1A) of the Income-tax Act, 1961 was only to prevent evasion of tax. He submits that when additional tax had clear and specific imprint of penalty, the Revenue could not be heard to say that the levy of additional tax is automatic under section 143(1A) of the Act. If additional tax could be levied in such circumstances, it would be punishing the assessee for no fault of his and that too without giving him a hearing.

7 Learned counsel for the Revenue submits that provision of section 143(1A) demonstrates that it is not penal in nature. It is the device to check evasion of tax. It is submitted that challenge to vires of section 143(1A) has been repelled by different High Courts and this court. Section 143(1A) has been inserted in the Income-tax Act so that the assessee may not be able to evade tax by resorting to the method of showing loss first and then reducing the loss. Learned counsel submits that the Division Bench of the High Court has rightly allowed the appeal of the Revenue upholding the demand of additional tax.

8 We have considered the submissions of the learned counsel for the parties and perused the records.

1. [1990] 182 ITR (St.) 1.

The only question to be answered in this appeal is as to whether the demand of additional tax under the provisions of section 143(1A) in the facts of the present case was justified or not. 9

Before we enter into the rival submissions of the learned counsel for the parties, it is relevant to have a look on the statutory scheme under sections 143 and 143(1A). Section 143(1)(a) reads thus : 10

"143.(1)(a) Where a return has been made under section 139, or in response to a notice under sub-section (1) of section 142,—

(i) if any tax or interest is found due on the basis of such return, after adjustment of any tax deducted at source, any advance tax paid and any amount paid otherwise by way of tax or interest, then, without prejudice to the provisions of sub-section (2), an intimation shall be sent to the assessee specifying the sum so payable, and such intimation shall be deemed to be a notice of demand issued under section 156 and all the provisions of this Act shall apply accordingly ; and

(ii) if any refund is due on the basis of such return, it shall be granted to the assessee :

Provided that in computing the tax or interest payable by, or refundable to, the assessee, the following adjustments shall be made in the income or loss declared in the return, namely—

(i) any arithmetical errors in the return, accounts or documents accompanying it shall be rectified ;

(ii) any loss carried forward, deduction, allowance or relief, which, on the basis of the information available in such return, accounts or documents, is prima facie admissible but which is not claimed in the return, shall be allowed ;

(iii) any loss carried forward, deduction, allowance or relief claimed in the return, which, on the basis of the information available in such return, accounts or documents, is prima facie inadmissible, shall be disallowed :

Provided further that where adjustments are made under the first proviso, an intimation shall be sent to the assessee, notwithstanding that no tax or interest is found due from him after making the said adjustments :

Provided also that an intimation under this clause shall not be sent after the expiry of two years from the end of the assessment year in which income was first assessable."

Sub-section (1A), as it originally read, was thus : 11

"143. (1A)(a) Where, in the case of any person, the total income, as a result of the adjustments made under the first proviso to clause (a) of sub-section (1), exceeds the total income declared in the return by any amount, the Assessing Officer shall,—

(i) further increase the amount of tax payable under sub-section (1) by an additional income tax calculated at the rate of twenty per cent of the tax payable on such excess amount and specify the additional income tax in the intimation to be sent under sub-clause (i) of clause (a) of sub-section (1) ;

(ii) where any refund is due under sub-section (1), reduce the amount of such refund by an amount equivalent to the additional income tax calculated under sub-clause (i)."

**12** Sub-section (1A) was amended by the Finance Act, 1993 with effect from April 1, 1989, which was the date upon which sub-section (1A) had been introduced into the Act. The substituted sub-section (1A) read thus :

"143. (1A)(a) Where as a result of the adjustments made under the first proviso to clause (a) of sub-section (1),—

(i) the income declared by any person in the return is increased ; or

(ii) the loss declared by such person in the return is reduced or is converted into income, the Assessing Officer shall,—

(A) in a case where the increase in income under sub-clause (i) of this clause has increased the total income of such person, further increase the amount of tax payable under sub-section (1) by an additional income tax calculated at the rate of twenty per cent on the difference between the tax on the total income so increased and the tax that would have been chargeable had such total income been reduced by the amount of adjustments and specify the additional income tax in the intimation to be sent under sub-clause (i) of clause (a) of sub-section (1) ;

(B) in a case where the loss so declared is reduced under sub-clause (ii) of this clause or the aforesaid adjustments have the effect of converting that loss into income, calculate a sum (hereinafter referred to as additional income tax) equal to twenty per cent of the tax that would have been chargeable on the amount of the adjustments as if it had been the total income of such person and specify the additional income tax so calculated in the intimation to be sent under sub-clause (i) of clause (a) of sub-section (1) ;

(C) where any refund is due under sub-section (1), reduce the amount of such refund by an amount equivalent to the additional income tax calculated under sub-clause (A) or sub-clause (B), as the case may be."

13 The amendments brought by the Finance Act, 1993 with retrospective effect, i. e., from April 1, 1989 are fully attracted with regard to assessment in question, i.e., for the assessment year 1991-92. The substituted sub-section (1A) makes it clear that where the loss declared by an assessee had been reduced by reason of adjustments made under sub-section (1)(a), the provisions of sub-section (1A) would apply. As noted above the Commissioner of Income-tax while rejecting the revision petition of the petitioner has taken the view that whenever adjustment is made, additional tax would be charged at 20 per cent. of the tax payable on such excess amount. The excess amount refers to the increase in the income and by implication the reduction in loss where even after the addition there is negative income. Whether there should be levy of additional tax in all circumstances and cases where loss is reduced, is the question to be answered in the present case.

14 By the Taxation Laws (Amendment) Act, 1991 in section 32, the third proviso was inserted to the following effect :

"Provided also that, in respect of the previous year relevant to the assessment year on the 1st day of April, 1991, the deduction in relation to any block of assets under this clause shall, in the case of a company, be restricted to seventy-five per cent of the amount calculated at the percentage, on the written down value of such assets, prescribed under this Act immediately before the commencement of the Taxation Laws (Amendment) Act, 1991."

15 Prior to insertion of the above proviso the depreciation was not restricted to 75 per cent. of the amount calculated at the percentage on the written down value of such assets. The return was filed by the assessee on December 31, 1991, prior to which date the Taxation Laws (Amendment) Act, 1991 had come into operation. It was due to a bona fide mistake and oversight that the assessee claimed 100 per cent. depreciation instead of 75 per cent. The 100 per cent. depreciation of Rs. 333,77,70,317 was claimed on written down value of assets, 25 per cent. depreciation was, thus, disallowed restricting it to 75 per cent. and after reducing 25 per cent. of the depreciation loss remained to the extent of Rs. (-) 3,43,94,90,393. Even as per reduction of 25 per cent. depreciation the return of loss income of the assessee remained. In claiming 100 per cent. depreciation the assessee claims that there was no intention to evade tax and the said claim was only

a bona fide mistake. As noted above by the Finance Act, 1993 section 143(1A) was substituted with retrospective effect from April 1, 1989. The Memorandum Explaining the Provisions of the Finance Bill with retrospective effect was to the following effect[1] :

> "The provisions of section 143(1A) of the Income-tax Act provide for levy of twenty per cent additional income tax where the total income, as a result of the adjustments made under the first proviso to section 143(1)(a), exceeds the total income declared in the return. These provisions seek to cover cases of returned income as well as returned loss. Besides its deterrent effect, the purpose of the levy of the additional income tax is to persuade all the assessees to file their returns of income carefully to avoid mistakes.
>
> In two recent judicial pronouncements, it has been held that the provisions of section 143(1A) of the Income-tax Act, as these are worded, are not applicable in loss cases.
>
> The Bill, therefore, seeks to amend section 143(1A) of the Income-tax Act to provide that where as a result of the adjustments made under the first proviso to section 143(1)(a), the income declared by any person in the return is increased, the Assessing Officer shall charge additional income tax at the rate of twenty per cent, on the difference between the tax on the increased total income and the tax that would have been chargeable had such total income been reduced by the amount of adjustments. In cases where the loss declared in the return has been reduced as a result of the aforesaid adjustments or the aforesaid adjustments have the effect of converting that loss into income, the Bill seeks to provide that the Assessing Officer shall calculate a sum (referred to as additional income tax) equal to twenty per cent of the tax that would have been chargeable on the amount of the adjustments as if it had been the total income of such person.
>
> The proposed amendment will take effect from April 1, 1989 and will, accordingly, apply in relation to the assessment year 1989-90 and subsequent years."

**16** Learned counsel for the Revenue has rightly submitted that object of section 143(1A) was the prevention of evasion of tax. The Memorandum Explaining the Provisions of the Finance Bill as noted above was also to persuade to the assessee to file the income-tax return carefully to avoid mistakes.

1. See [1993] 200 ITR (St.) 140.

This court in *CIT* v. *Sati Oil Udyog Limited* [2015] 7 SCC 304[1], had occasion to consider elaborately the provisions of section 143(1A), its object and validity. There was a challenge to the retrospectivity of the provisions of section 143(1A) as introduced by the Finance Act, 1993. The Gauhati High Court[2] had held that the retrospective effect given to the amendment would be arbitrary and unreasonable. The appeal was filed by the Revenue in this court in which appeal, this court had occasion to examine the constitutional validity of the provisions. This court in the above judgment held that object of section 143(1A) was the prevention of evasion of tax. In paragraph 9 of the judgment following has been laid down[3] : **17**

> "On a cursory reading of the provision, it is clear that the object of section 143(1A) is the prevention of evasion of tax. By the introduction of this provision, persons who have filed returns in which they have sought to evade the tax properly payable by them is meant to have a deterrent effect and a hefty amount of 20 per cent. as additional income tax is payable on the difference between what is declared in the return and what is assessed to tax."

Relying on earlier judgment of this court in *K. P. Varghese* v. *ITO* [1981] 4 SCC 173[4], this court in the above case held that provisions of section 143(1A) should be made to apply only to tax evaders. In paragraphs 21 and 25 following was laid down[5] : **18**

> "In the present case, the question that arises before us is also as to whether bona fide assessees are caught within the net of section 143(1A). We hasten to add that unlike in *J. K. Synthetics* v. *Asst. CIT*[6] case, section 143(1A) has in fact been challenged on constitutional grounds before the High Court on the facts of the present case. This being the case, we feel that since the provision has the deterrent effect of preventing tax evasion, it should be made to apply only to tax evaders. In support of this proposition, we refer to the judgment in *K. P. Varghese* v. *ITO*. The court in that case was concerned with the correct construction of section 52(2) of the Income-tax Act: (*K. P. Varghese* case, SCC page 179, para 4 : SCR page 639[7] :
>
> 'Without prejudice to the provisions of sub-section (1), if in the opinion of the Income-tax Officer the fair market value of a capital

1. [2015] 372 ITR 746 (SC).
2. *Sati Oil Udyog Ltd.* v. *CIT* [1998] 232 ITR 502 (Gauhati) and *CIT (Deputy) (Asstt.)* v. *Ashok Paper Mills Ltd.* [2002] 256 ITR 673 (Gauhati).
3. page 753 of 372 ITR.
4. [1981] 131 ITR 597 (SC).
5. page 759 of 372 ITR.
6. [2001] 251 ITR 200 (SC).
7. page 603 of 131 ITR.

asset transferred by an assessee as on the date of the transfer exceeds the full value of the consideration declared by the assessee in respect of the transfer of such capital asset by an amount of not less than fifteen per cent of the value declared, the full value of the consideration for such capital asset shall, with the previous approval of the Inspecting Assistant Commissioner, be taken to be its fair market value on the date of its transfer.'

Taking a cue from *Varghese* case, we therefore, hold that section 143(1A) can only be invoked where it is found on facts that the lesser amount stated in the return filed by the assessee is a result of an attempt to evade tax lawfully payable by the assessee. The burden of proving that the assessee has so attempted to evade tax is on the Revenue which may be discharged by the Revenue by establishing facts and circumstances from which a reasonable inference can be drawn that the assessee has, in fact, attempted to evade tax lawfully payable by it. Subject to the aforesaid construction of section 143(1A), we uphold the retrospective clarificatory amendment of the said section and allow the appeals. The judgments of the Division Bench of the Gauhati High Court are set aside. There will be no order as to costs."

**19** This court in the above case upheld the Constitutional validity of section 143(1A) (as inserted by the Finance Act, 1993) subject to holding that section 143(1A) can only be invoked where it is found on facts that the lesser amount stated in the return filed by the assessee is a result of an attempt to evade tax lawfully by the assessee.

**20** Applying the ratio of the above judgment in the present case, we need to find out as to whether 100 per cent. depreciation as mentioned in the return filed by the assessee was a result of an attempt to evade tax lawfully payable by the assessee.

**21** We have seen from the facts, as noted above, that even after disallowing 25 per cent. of the depreciation, the assessee in the return remained in loss and the 100 per cent. depreciation was claimed by the assessee in the return due to a bona fide mistake. By Taxation Laws (Amendment) Act, 1991, the depreciation in the case of company was restricted to 75 per cent. which due to oversight was missed by the assessee while filing the return. The Commissioner of Income-tax by deciding the revision petition has also not made any observation to the effect that 100 per cent. depreciation claimed by the assessee was with an intent to evade payment of tax lawfully payable by the assessee, rather the Commissioner in his order dated March 31, 1992 has observed that whenever adjustment is made, additional

tax has to be charged at 20 per cent. of the tax payable on such excess amount.

It is true that while interpreting a Tax Legislature the consequences and **22**
hardship are not looked into but the purpose and object by which taxing statutes have been enacted cannot be lost sight. This court while considering the very same provision, i.e., section 143(1A), its object and purpose and while upholding the provision held that the burden of proving that the assessee has attempted to evade tax is on the Revenue which may be discharged by the Revenue by establishing facts and circumstances from which a reasonable inference can be drawn that the assessee has, in fact, attempted to evade tax lawfully payable by it. In the present case, not even a whisper, that claim of 100 per cent. depreciation by the assessee, 25 per cent. of which was disallowed was with intent to evade tax. We cannot mechanically apply the provisions of section 143(1A) in the facts of the present case and in view of the categorical pronouncement by this court in *CIT* v. *Sati Oil Udyog Limited*[1], where it is held that section 143(1A) can only be invoked when the lesser amount stated in the return filed by the assessee is a result of an attempt to evade tax lawfully payable by the assessee. In view of the above, we hold that mechanical application of section 143(1A) in the facts of the present case was uncalled for.

In the result, we allow the appeal, set aside the judgment of the Division **23**
Bench of the High Court as well as demand of additional tax dated February 12, 1992 as amended on February 28, 1992.

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**[2020] 424 ITR 715 (Bom)**

[In the Bombay High Court]

## ASSET RECONSTRUCTION COMPANY INDIA PVT. LTD.

*v.*

## DEPUTY COMMISSIONER OF INCOME-TAX AND OTHERS

**Akil Kureshi** and **M. S. Sanklecha** JJ.

January 24, 2019.

**SS ▸ ITA 1961, ss 147, 148**
**AY ▸ 2011-12**
**HF ▸ Assessee**

Reassessment—Notice after four years—Assessee purchasing non-performing asset from bank and receiving payment from

1. [2015] 372 ITR 746 (SC).

ENTITY ALLEGED TO HAVE HAD DUBIOUS DEALINGS WITH BOGUS ENTRY PROVIDER—NO LIVE LINK BETWEEN INFORMATION AND BELIEF THAT INCOME HAD ESCAPED ASSESSMENT—REASONS NOT SUPPORTED BY AFFIDAVIT OR ORAL SUBMISSION—NOTICE OF REASSESSMENT INVALID—INCOME-TAX ACT, 1961, SS. 147, 148.

*The notice under section 148 of the Income-tax Act, 1961 for reopening of the assessment under section 147 has to be judged only on the basis of the reasons recorded by the Assessing Officer. When the reasons do not record any other element of income chargeable to tax having escaped assessment, it would not be possible for the Department to bring such element into consideration either through affidavit or oral arguments.*

*The assessee was engaged in the business of securitisation and asset reconstruction and acted as trustees for the non-performing financial assets acquired from various banks and financial institutions. For the assessment year 2011-12, the Assessing Officer passed an order under section 143(3). After a period of four years, the Assessing Officer issued a notice under section 148 for reopening the assessment under section 147. He recorded reasons that he had received information from the Investigation Wing that SCS was a main person who was engaged in providing bogus accommodation entries through several companies controlled by him, that it was found that the assessee had entered into transactions with A, that the assessee had purchased non-performing assets of A from a bank in the year 2009, that against this A had paid a sum of Rs. 2.70 crores to the assessee, that A was engaged in providing bogus accommodation entries at the instance of SCS and that on the basis of such information, the Assessing Officer was prima facie of the view that the assessee had dealings with A which inturn had indulged in dealing with various accommodation entries and therefore, income chargeable to tax of Rs. 2.70 crores had escaped assessment. The objections raised by the assessee were rejected. On a writ petition :*

Held, *allowing the petition, that the reasons recorded for reopening the assessment did not provide the live link to the formation of belief by the Assessing Officer that the assessee's income chargeable to tax had escaped assessment. The assessee having purchased the non-performing assets from the bank had received the payment of Rs. 2.70 crores from A. This had nothing to do with the alleged dubious dealings of A at the instance of SCS the bogus entry provider. The very formation of the belief by the Assessing Officer that income chargeable to tax in the hands of the assessee had escaped assessment lacked validity.*

*[The Supreme Court has dismissed the special leave petition filed by the Department against this judgment : see* [2019] 416 ITR (St.) 134.*]*

Hindustan Lever Ltd. *v.* R. B. Wadkar, Asst. CIT (No. 1) [2004] 268 ITR 332 (Bom) *relied on*.

Hindustan Lever Ltd. *v.* R. B. Wadkar, Asst. CIT (No. 1) [2004] 268 ITR 332 (Bom) (para 8) *referred to*.

**Writ Petition No. 3493 of 2018.**

*Jitendra Jain* instructed by *Atul Jasani* for the petitioner.

*N. C. Mohanty* for the respondents.

**JUDGMENT**

Rule having been issued previously, we have heard learned counsel for the parties on final hearing. 1

The petitioner has challenged a notice of reopening of assessment dated March 30, 2018. 2

The brief facts are as under : 3

The petitioner-Asset Reconstruction Company India Private Limited ("ARCIL" for short) and is engaged in the business of securitisation and asset reconstruction and also acts as trustees for the non-performing financial assets acquired from the various banks and financial institutions.

For the assessment year 2011-12, the petitioner had filed return of income on September 30, 2011 declaring income of Rs. 79.23 crores. The return was taken in scrutiny by the Assessing Officer who passed the order of assessment under section 143(3) of the Income-tax Act, 1961 ("the Act" for short) on March 25, 2014. To reopen such assessment the Assessing Officer issued the impugned notice which as can be seen was done beyond the period of four years from the end of the assessment year. In order to issue the notice, the Assessing Officer had recorded the following reasons : 4

> "The assessee, M/s. Asset Reconstruction Company India Pvt. Ltd. assessed with the charge of the ACIT 6(1)(2), Mumbai, filed its return of income on October 14, 2010 at Rs. 86,82,25,240. Assessment under section 143(3) of the Act was completed on March 26, 2013 determining the total income at Rs. 89,66,70,995 as per ITD system.
>
> 2. Vide letter dated March 25, 2017, the Deputy Commissioner of Income-tax, CC 2(2), Mumbai has informed that M/s. Asset Reconstruction Company India Pvt. Ltd. has had dealings with M/s. Avance Technologies Ltd. which was indulged in providing bogus accommodation entries. The copy of the said letter dated March 25, 2017 is enclosed for ready reference.

3. As per letter dated March 25, 2017, a search under section 132 of the Act was carried out at the residence and various premises of Shri Shirish C. Shah who happened to be the main person engaged in providing bogus accommodation entries like long-term capital gain, share capital with huge share premium, turnover, loan etc. Shri Shirish C. Shah, directly and indirectly controlled more than 200 companies which included some of the public limited companies also. An enquiry was made with M/s. Asset Reconstruction Company India Pvt. Ltd. regarding the nature of transactions with M/s. Avance Technologies Ltd. during the financial year 2010-11 (relevant to the assessment year 2011-12). M/s. Asset Reconstruction Company India Pvt. Ltd. explained that they had purchased the non-performing assets (NPA) of M/s. Avance Technologies Ltd. from Allahabad Bank in the year 2009. Against the same, M/s. Avance Technologies Ltd. had paid Rs. 2.70 crores to M/s. Asset Reconstruction Company India Pvt. Ltd. However, as M/s. Avance Technologies Ltd. was engaged in providing bogus accommodation entries to various parties in connivance with Shri Shirish C. Shah, the claim of M/s. Asset Reconstruction Company India Pvt. Ltd. may be investigated.

4. In view of the above and based on the material evidence available on record, prima facie, it is seen that the assessee, M/s. Asset Reconstruction Company India Pvt. Ltd. has had dealings with Avance Technologies Ltd., which was indulged in providing bogus accommodation entries and that income chargeable to tax to the tune of Rs. 2.70 crores has escaped assessment in the financial year 2010-11, i.e., the assessment year 2011-12.

5. In view of the above, I have reason to believe that income chargeable to tax has escaped assessment within the meaning of section 147 of the Income-tax Act, 1961 on account of the above mentioned transaction and that this escapement is due to the failure of the assessee-company to disclose fully and truly all material facts relevant to the determination of its correct income.

It is clear from the above that the income chargeable to tax has escaped assessment for the amount of one lakh rupees or more in this assessment year 2011-12.

Thus, I am satisfied that this is a fit case for issue of notice under section 148 of the Income-tax Act, 1961. Accordingly, the case may kindly be reopened under section 147 of the Income-tax Act, 1961 and notice under section 148 may be issued to bring to tax the income so escaped for the assessment year 2011-12."

Upon being supplied the reasons, the assessee raised objections to the notice of reopening by the letter dated September 24, 2018 and October 17, 2018. Such objections were however rejected by an order dated October 3, 2018 by the Assessing Officer. Hence the petition. 5

We have heard the learned counsel for the parties at considerable length. If we peruse the reasons, the stand of the Assessing Officer is that he received information from the Investigation Wing that one S.C. Shah is the main person who is engaged in providing bogus accommodation entries through several companies controlled by him. It was found that ARCIL had entered into transactions with one M/s. Avance Technologies Limited ("Avance" for short). ARCIL had purchased non-performing assets (NPA) of the said Avance from Allahabad Bank in the year 2009. Against this, Avance had paid a sum of Rs. 2.70 crores to ARCIL. According to the information of the Assessing Officer, Avance was engaged in providing bogus accommodation entries at the instance of the said S. C. Shah. On the basis of such information, the Assessing Officer was prima facie of the view that the assessee, i.e., ARCIL has dealing with Avance which inturn has indulged in dealing with various accommodation entries and therefore, income chargeable to tax of Rs. 2.70 crores had escaped assessment. 6

In our opinion, the very premise of the Assessing Officer to form a belief that income chargeable to tax had escaped assessment is completely invalid. As per the information received by the Assessing Officer and to which the assessee raised its no dispute, the assessee had as an asset reconstruction company dealt with Avance. Avance was a borrower in Allahabad Bank. The assessee purchased non-performing assets from Allahabad Bank. By way of recovery, Avance paid a sum of Rs. 2.70 crores to the assessee. Whatever be the nature of existence of Avance, its dealings with other individual entities and dealings of said S. C. Shah, we simply fail to appreciate how the Assessing Officer in the present case asserts that in the case of the assessee income chargeable to tax has escaped assessment. Even going by the information at the command of the Assessing Officer, the assessee having purchased the non-performing assets from Allahabad Bank, received the payment of Rs. 2.70 crores from Avance. This has nothing to do with the alleged dubious dealings of Avance at the instance of S. C. Shah. In clear terms, the very formation of the belief by the Assessing Officer that income chargeable to tax in the hands of the assessee had escaped assessment, lacks validity. 7

The Department as well as the counsel for the Revenue have tried to improve upon the reasons stated by the Assessing Officer by suggesting 8

that it would be necessary to verify whether such income was offered to tax by the assessee or whether the trustee for whom the assessee claims would have received the income had offered the same to tax. None of these elements find place in the reasons recorded by the Assessing Officer. As is well settled by a series of judgments of various courts ; that notice of reopening of the assessment can be supported on the basis of the reasons recorded by the Assessing Officer for this purpose. Reliance can be placed on the decision of the court in the case of *Hindustan Lever Ltd.* v. *R. B. Wadkar, Asst. CIT* [2004] 268 ITR 332 (Bom). Thus, the notice of reopening of the assessment need to be judged only on the basis of the reasons recorded by the Assessing Officer. When the reasons do not record any other element of income chargeable to tax having escaped assessment, it would not be possible for the Revenue to bring such element into consideration either through affidavit or oral arguments. We have examined the reasons and find that these reasons simply do not provide the live link to the formation of belief by the Assessing Officer that the assessee's income chargeable to tax has escaped assessment. In the result, the impugned notice is set aside. The petition is disposed of.

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