IN THE HIGH COURT OF JUDICATURE AT BOMBAY

ORDINARY ORIGINAL CIVIL JURISDICTION

WRIT PETITION NO.892 OF 2010

3i Infotech Limited, a company
incorporated under the Companies
Act, 1956 and having its registered
office at Tower No.5, 3rd to 6th floor,
International Infotech Park, Vashi,
Navi Mumbai – 400 075 .....Petitioner

Versus

1. The Assistant Commissioner of
Income-tax – 10(3), having his
office at Aaykar Bhavan,
M.K. Road, Mumbai – 400 020

2. The Commissioner of Income-tax – 10
having his office at Aayakar Bhavan,
M.K. Road, Mumbai – 400 020.

3. The Union of India, through
the Secretary, Department of
Revenue, Ministry of Finance,
North Block, New Delhi – 110 001 .....Respondents.

Mr.Percy J. Pardiwala, Senior Advocate with Mr.Atul K. Jasani for the petitioner.

Mr.Vimal Gupta for the respondents.

CORAM : Dr.D.Y. Chandrachud &
J.P. Devadhar, JJ.

DATE : 14 June, 2010.

ORAL JUDGMENT (Per Dr.D.Y. Chandrachud, J.)

1. Rule. With the consent of Counsel, rule is made returnable forthwith. By consent of Counsel for both the parties, the petition is taken up for hearing and final disposal.

2. The dispute in these proceedings arises out of a notice issued by the first respondent on 18 March 2009 by which an assessment for assessment year 2002-2003 is sought to be re-opened in pursuance of the provisions of Section 147 of the Income Tax Act, 1961. The notice for re-opening the assessment is beyond a period of four years from the end of the relevant assessment year.

3. The assessee filed a return of income for assessment year 2002-2003 on 30 October 2002 declaring a loss of Rs.46.96 lakhs and computed tax under Section 115JB of Rs.1.94 crores. An order of assessment was passed on 7 March 2005 under Section 143(3). On 18 March 2009, the Assessing Officer issued a notice under Section 148. The reasons on the basis of which the assessment is sought to be re-opened are stated in the notice and are as follows :

> "The assessee has filed its original return of income on 31-10-2002. Assessment u/s. 143(3) was completed 7-3-2005 computing income at Rs.9,79,34,208/-.
>
> It is seen from the assessment records that as per Clause 2.18 of Notes of Accounts the company has engaged ICICI Infotech Inc. USA, the wholly owned subsidiary for providing market development and sales support in the US for project software and implementation services for onsight projects effective July 1, 2001. As per the arrangement, the company remunerates Infotech Inc. on a cost plus basis for the aforesaid services and all the project revenues accrue to the company. Out of such remuneration amount payable towards market development and support expenses of Rs.218.54 million has been treated as deferred over a period of two years as in the opinion of the management benefit of such expenses would accrue in future also. The company has amortized Rs. 9,36,63,726/- out of the said amount of Rs.21,85,48,694/- in the Accounts and also claim deduction of Rs.21,85,48,694/- in computation of income while adding back the amortized amount. However, the said expenditure should have been treated as capital expenditure and the assessee has wrongly claimed the deduction towards such expenses.
>
> Thus there is an escapement of income to this extent of Rs.21.85 cr.
>
> 2. Further, it is also seen that the assessee has arrived at Loss on sale of long term investment amounts to Rs.2.4 million

whereas the amount added back to the income is only Rs.1.85 million.

Thus there is an escapement of income to this extent of Rs.60 lacs.

3. It is seen from Annexure 8 to Clause 20 & 22(b) of Form 3CD that an amount of Rs.31,32,627/- has been debited to P & L Account on account of prior period expenses which are not allowable as per provisions of I.T. Act. The same should have been added back.

Thus there is an escapement of income to this extent of Rs.31.32 lacs.

4. The assessee has debited Rs.126.80 million on account of interest on fixed loan to P & L Account which has not been capitalized. The company has capitalized Rs.21.89 million in P.Y. 00-01 on the same account.

Thus there is an escapement of income to this extent.

Thus there is a failure on the part of the assessee to disclose fully and truly all material facts necessary for his assessment, for the said assessment year. I have reasons to believe that the income to the extent of Rs.22.22 cr. has been escaped the assessment."

4. The petitioner furnished its objections to the re-opening of the assessment. An order of assessment was passed on 30 November 2009 without disposing of the objections. In a petition instituted before this Court under Article 226 of the Constitution, a Division Bench by its order dated 10 March 2010 observed that in failing to deal with the objections of the assessee, the Assessing Officer had not complied with the directions of the Supreme Court in ***G.K.N. Drive Shaft (India) Limited V/s. Income Tax Officer***[1]. While setting aside the order of re-assessment, this Court directed the Assessing Officer to pass an order on the objections of the assessee. On

1 259 ITR 19 (SC)

remand, the Assessing Officer has not dealt with the merits of the objections holding that it is at the stage of assessment that he would be dealing with these objections.

5. In assailing the exercise of the jurisdiction under Section 147, the learned Counsel appearing on behalf of the assessee submitted that : (i) There was a full disclosure by the assessee of all the material facts necessary for the assessment. The re-opening of the assessment is after four years of the end of the relevant assessment year. There was no failure to disclose fully and truly all the material facts necessary for the assessment. Hence, the condition precedent to the exercise of the jurisdiction to re-open the assessment beyond four years has not been fulfilled; (iii) Four reasons have weighed with the Assessing Officer in re-opening the assessment. On each of the four issues, there was a full and true disclosure of all the material facts by the assessee for the assessment. As a matter of fact, the reasons which have been furnished for re-opening the assessment are based on the assessment record and on the disclosures made by the assessee. Hence, the condition precedent to a valid exercise of the power to re-open an assessment beyond four years does not exist in the present case and hence the exercise of the writ jurisdiction under Article 226 would be warranted.

On the other hand, it has been urged on behalf of the Revenue that (i) Save and except for the first issue on which the assessment is sought

to be re-opened, the other three issues were not considered by the Assessing Officer; (ii) Explanation (1) to Section 147 provides that a mere production before the Assessing Officer of account books or other evidence from which material evidence could with due diligence have been discovered will not necessarily amount to a disclosure within the meaning of the first proviso to Section 147; (iii) The proviso would apply in a situation such as the present where, according to the Revenue, the Assessing Officer has not considered three of the issues on the basis on which the assessment was sought to be re-opened.

6. Section 147 of the Income Tax Act, 1961 empowers the Assessing Officer to assess or re-assess income chargeable to tax which he has reason to believe has escaped assessment and other income which comes to his notice subsequently during the course of the proceedings under the Section. The existence of a reason to believe conditions a valid exercise of statutory power under Section 147. The proviso however stipulates that where an assessment has been carried out under sub-section (3) of Section 143, action after the expiry of four years from the end of the relevant assessment year would stand barred unless income chargeable to tax has escaped assessment inter alia by the failure on the part of the assessee to disclose fully and truly all material facts necessary for the assessment for that assessment year. Hence, where a re-opening of assessment takes place beyond a period of four years from the end of the relevant assessment year, the test which the statute requires to be

applied is based on the nature of the disclosure that is made by the assessee. If the assessee has made a full and true disclosure of all the material facts for his assessment, the action of re-opening the assessment would stand barred. Contrariwise, where there is a failure on the part of the assessee to disclose fully and truly all material facts necessary for the assessment, the re-opening of the assessment would stand validated even if it takes place beyond the expiry of a period of four years.

7. Explanation (1) to Section 147 stipulates that the 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 a disclosure within the meaning of the first proviso. In other words, an assessee cannot rest content merely with the production of account books or other evidence during the course of the assessment proceedings and challenge the re-opening of the assessment on the ground that if the Assessing Officer were to initiate a line of enquiry, he could with due diligence have arrived at material evidence. The primary obligation to disclose is on the assessee and the burden of making a full and true disclosure of material facts does not shift to the Assessing Officer. The assessee has to disclose fully and truly all material facts. Producing voluminous records before the Assessing Officer does not absolve the assessee of the obligation to disclose and the assessee, therefore, cannot be heard to say that if the Assessing Officer were to conduct a further

enquiry, he would come into possession of material evidence with the exercise of due diligence. An assessee cannot throw reams of paper at the Assessing Officer and rest content in the belief that the Officer better beware or ignore the hidden crevices in the pointed material at his peril.

8. Parliament has used the words necessarily in explanation (1). The expression '*necessarily*' means *inevitably* or as a matter of a compelling inference. The Oxford English Dictionary defines the expression "*necessarily*" as meaning (i) By force of necessity; unavoidably; (ii) As a necessary aid or concomitant; indispensably; (iii) By a necessary connexion; (iv) In accordance with a necessary law or operative principle; (v) As a necessary result or consequence; and (vi) Of necessity; inevitably. The production of account books or other evidence before the Assessing Officer will not, therefore, inevitably amount to an inference of disclosure within the meaning of the first proviso. As a Division Bench of the Calcutta High Court observed in ***Imperial Chemicals Industries Limited V/s. Income-Tax Officer***[2], the words 'not necessarily' indicate that "whether it is a disclosure or not within the meaning of the said Section .. would depend on the facts and circumstances of each case, that is the nature of the document and circumstances in which it is produced." (at page 639). In ***Rakesh Agarwal Vs. Assistant Commissioner of Income Tax***[3], the Delhi High Court held that the nature of the documents and the circumstances in which these are

2 (1978) 111 ITR 614 (Cal.)
3 (1996) 221 ITR 492 (Del.)

produced before the Assessing Officer will determine the question. If the material is not writ large on the document, but is embedded in voluminous records or books of account which require careful scrutiny by the Assessing Officer, it is quite possible that having regard to the nature of the documents, material evidence cannot be discovered from such records despite due diligence and the case would attract the Explanation.

9. In this background, it would now be necessary to consider each of the four reasons which have weighed with the Assessing Officer in re-opening the assessment.

The first ground on which the assessment is sought to be re-opened is that the assessee had engaged a wholly owned subsidiary for providing market development and sales support in the US. The subsidiary was being remunerated on a cost plus basis. Out of such remuneration, expenses amounting to Rs.218.54 million (Rs.21.85 crores) were treated as deferred over a period of two years. The assessee had amortized Rs.9.36 crores out of the amount of Rs.21.85 crores. According to the Assessing Officer the assessee had claimed a deduction of Rs.21.85 crores in the computation of income while adding back the amortized amount. However, the expenditure should have been treated as capital expenditure and the assessee is stated to have wrongly claimed the deduction towards such expenses. On this ground, it has been stated that there has been an

escapement of income to the extent of Rs.21.85 crores.

10. Now in considering the first ground on which the assessment is sought to be re-opened reference may be made at the outset to Schedule 12 of the Schedules forming part of the accounts of the assessee. The assessee disclosed that the market development and support expenses were amortized to the extent of Rs.9.36 crores. In Schedule 9 the deferred revenue expenditure for market development and support expenses reflected an addition of Rs.21.85 crores during the year. Rs.9.36 crores was amortized during the year and was charged to the profit and loss account leaving a balance of Rs.12.84 crores to be carried forward to the next year. The basis on which this was done was explained in para 2.18 of the Significant Accounting Policies and Notes to the Accounts. The statement of total income of the assessee included an amount of Rs.9.36 crores which was added back as an item not allowable or considered separately. An amount of Rs.21.85 crores was deducted as market development and support expenses. Note 5 of the Notes attached to and forming part of the return contained a disclosure to the effect that market development and support expenditure amounting to Rs.21.85 crores has been claimed as a deduction in the year at incurring.

11. During the course of the proceedings, the Assessing Officer addressed a communication dated 3 December 2004 to the assessee seeking

inter alia a disclosure together with documentary evidence in relation to market development and support expenses which were amortized. The Assessing Officer in Item 15 of the letter specifically brought his attention to bear on the fact that the assessee had incurred market development expenditure at Rs.21.85 crores and that in the profit and loss account expenses to the extent of Rs.9.36 crores have been debited as expenses amortized while the balance was deferred as Revenue expenditure. The Assessing Officer noted that in the computation of total income, the entire expenditure of Rs.21.25 crores has been claimed as a deduction. The Petitioner was called upon to explain why there was a differential treatment of the expenses in the profit and loss account vis-a-vis the computation of income and to show cause as to why the balance of Rs.12.49 crores should not be added back to the total income of the assessee. In response to the questionnaire the assessee furnished a detailed note to the Assessing Officer by a letter dated 7 February 2005. In the course of its response the assessee clarified that during the year it had paid an amount of Rs.21.85 crores to its subsidiary and though the same was treated as deferred revenue expenditure in the books of account and amortized over a period of two years, the entire amount had been claimed as an expenditure. The assessee relied upon certain decisions in support of its case. It was after the assessee had filed its response that an order of assessment was passed by the Assessing Officer.

12. The record before the Court, to which a reference has been

made earlier, is clearly reflective of the position that during the course of the assessment proceedings the assessee had made a full and true disclosure of all material facts in relation to the assessment. As a matter of fact, it would be necessary to note that the notice to re-open the assessment on the first issue is founded entirely on the assessment records. There is no new material to which a reference is to be found and the entire basis for re-opening the assessment is the disclosure which has been made by the assessee in the course of the assessment proceedings. In ***Cartini India Limited V/s. Additional Commissioner of Income Tax***[4], a Division Bench of this Court has observed that where on consideration of material on record, one view is conclusively taken by the Assessing Officer, it would not be open to the Assessing Officer to re-open the assessment based on the very same material with a view to take another view. The principal which has been enunciated in Cartini must apply to the facts of a case such as the present. The assessee had during the course of the assessment proceedings made a complete disclosure of material facts. The Assessing Officer had called for a disclosure on which a specific disclosure on the issue in question was made. In such a case, it cannot be postulated that the condition precedent to the re-opening of an assessment beyond a period of four years has been fulfilled.

13. In so far as the second ground for re-opening the assessment is concerned, the Assessing Officer has adverted to the fact that the assessee

4 (2009) 314 ITR 275 (Bom)

arrived at a loss on sale of long term investments at Rs.2.4 million (the correct figure as a matter of fact should read as Rs.2.04 million) whereas the amount added back to the income was Rs.1.85 million. The balance, according to the Assessing Officer reflects an escapement of income. Now, in so far as this aspect is concerned it is evident from Schedule 12 to the profit and loss account that the assessee, as part of its selling general and administrative expenses disclosed a loss on sale of long term investments of Rs.2.04 million. In Schedule 13 under the head of other income, the assessee disclosed a profit on the sale of current investments of Rs.0.18 million. The statement of total income of the assessee contains an addition of a net amount of Rs.1.85 million on account of the loss on investments. This represents the netting off of the loss of Rs.2.04 million against a profit of Rs. 0.18 million against the sale of current investments. The learned Counsel appearing on behalf of the Revenue urged during the course of submissions that from the statement of total income it is not clear as to how the loss in the amount of Rs.1.85 million on the sale on investments is accounted for and whether this forms a part of the capital loss of Rs.2.80 million which is to be carried forward. The difficulty in accepting the line of submission urged on behalf of the Revenue is that this is not the reason which have weighed with the Assessing Officer when the assessment was sought to be re-opened. The validity of the re-opening of the assessment has to be determined with reference to the reasons which have weighed with the Assessing Officer. Those norms cannot be added to or supported on a basis which was not

present to the mind of the Assessing Officer when he issued the notice to re-open. That apart, when this Court by its judgment dated 10 March 2010 found that the Assessing Officer had passed an order of assessment without dealing with the objections of the assessee, in breach of the judgment of the Supreme Court in G.K.N. Drive Shaft, an opportunity was granted to the Assessing Officer to deal with the objections of the assessee. The Assessing Officer in the order that he thereafter passed on 5 April 2010 has not dealt with the objections of the assessee and has on the contrary held that the merits of the objections would be decided only at the stage of the assessment proceedings. Consequently, neither in the reasons advanced by the Assessing Officer for re-opening the assessment nor in the order passed on the objections filed by the assessee is there any reference to the ground which has been urged in the submissions on behalf of the Revenue at the hearing of these proceedings. A ground which has no basis either in the notice for re-opening the assessment or in the order dealing with the objections of the assessee cannot be heard to be urged for the first time in these proceedings, instituted under Article 226 of the Constitution to challenge the re-opening of the assessment.

14. The third ground on which the assessment has been sought to be re-opened is that from Annexure 2, Clauses 20 and 22(b), of Form 3CD an amount of Rs.31.32 lakhs is found to be debited to the profit and loss account on account of prior period expenses. This according to the Assessing Officer

is not allowable under the Act and should be added back. To this extent, the Assessing Officer has found that there was an escapement of income. During the course of the submissions, the attention of the Court has been drawn by the learned Counsel appearing on behalf of the assessee to the Particulars of income and expenditure of the prior period, credited or debited to the profit and loss account. Appended to the statement are the following notes :

> "1) Based on the recommendations of the Institute of Chartered Accountants of India in its publication "Guidance Note on Tax Audit u/s.44AB of Income Tax Act, 1961" at para 44.2 of edition Sept 99, expenditure of earlier years means expenditure which arose or accrued in any earlier year and which excludes any expenditure of any earlier year for which the liability to pay has crystallized during the year.
>
> 2) Excess / short provision of earlier year & income and expenditure crystallized during the year though shown above has not been considered as prior period item."

15. These notes, according to the assessee are consistent with the Guidance Note issued by the Institute of Chartered Accountants on Tax Audit under Section 44AB of the Act. By its note, the assessee has recorded that the expenditure of the earlier years means expenditure which arose or which accrued in any earlier year and excludes any expenditure of an earlier year for which the liability to pay has crystallized during the year. Similarly, the assessee has clarified that excess / short of provision of an earlier year and income and expenditure crystallized during the year, though shown in the statement, have not been considered as prior period items. The assessee, as the material on record would show, therefore brought to bear the attention of

the Assessing Officer to this facet while submitting the Tax Audit Report as a part of its return of income. This is not a case where the assessee can be regarded as having merely produced its books of account or other evidence during the course of the assessment proceedings on the basis of which material evidence could have been deduced by the Assessing Officer with the exercise of due diligence. Under Section 139 the assessee was under a mandatory obligation to furnish with its return of income the report of audit under Section 44AB. The assessee fulfilled the obligation. The disclosures which are made as part of the report under Section 44AB cannot fall file within the interdict of explanation (1) to Section 147.

16. In so far as the fourth ground for re-opening the assessment is concerned, the Assessing Officer has noted that the assessee debited an amount of Rs.12.68 crores on account of the interest on a fixed loan to the profit and loss account which has not been capitalized. The assessee is noted to have capitalized an amount of Rs.2.18 crores in the previous year 2000-2001 on the same account. As regards this ground it would be important to note that the assessee had disclosed as part of its profit and loss account earnings before interest, depreciation and tax at Rs.58.09 crores. The profit before tax was computed at Rs.33.29 crores, after deducting from the aforesaid amount the interest on a fixed loan of Rs.12.68 crores and amortization of premium on debentures at Rs.12.11 crores. As part of its disclosure of Significant Accounting Policies, in Schedule 14 the assessee

disclosed in para 1.9 under the heading 'Borrowing Costs' that borrowing costs directly attributable to acquisition, construction and production of assets are capitalized as part of the costs of such asset upto the date of completion. In its objections to the re-opening of the assessment, the assessee also noted that under Section 36(1)(iii), the interest paid in respect of capital borrowed for the purposes of business or production is allowable as a deduction. Interest expenses of Rs.12.68 crores debited to the profit and loss account were disclosed to constitute interest paid on loans taken for carrying out normal business activities and was claimed as an allowable deduction under Section 36(1)(iii). The assessee drew the attention of the Assessing Officer to the fact that interest expenses of Rs.2.18 crores referred to in the notice for re-opening was capitalized in the previous year 2000-2001 because they were incurred in respect of a loan taken for acquisition of fixed assets. This explanation of the assessee was evidently not considered and has not been dealt with while disposing of the objections raised by the assessee to the re-opening of the assessment.

17. For these reasons, we are of the view that the Revenue has failed to establish before the Court that there was a failure on the part of the assessee to disclose fully and truly all the material facts necessary for the assessment for assessment year 2002-2003. Unless this were to be the case, the exercise of the power to re-open the assessment beyond a period of four years of the end of the relevant assessment year would fail to fulfill the

statutory condition precedent to a valid exercise of the power to re-open an assessment beyond a period of four years.

18. Consequently, the petition would have to be allowed and is accordingly allowed. Rule is made absolute in terms of prayer clause (a) by setting aside the notice dated 18 March 2009. There shall be no order as to costs.

(J.P. Devadhar, J.) (Dr.D.Y. Chandrachud, J.)