Income Tax Appellate Tribunal - Delhi
Fisons Ispat Ltd. vs Assistant Commissioner Of ... on 29 May, 1992
Equivalent citations: 1992 42 ITD 365 Delhi
Bench: R Mehta
ORDER R.M. Mehta, Accountant Member

1. These appeals are directed against separate orders passed by the CIT under Section 263 and as they have been heard together and the points involved are also identical, I dispose them of by means of a consolidated order. The subsequent discussion pertains to the appeal of Fisons Ispat Ltd. in ITA No. 3074 (Del.)/91.

2. For the assessment year 1987-88, the previous year in respect of which ended on 30th June 1986, the assessee-company filed its return on 19th June 1987 declaring an income of Rs. 54,392. The assessment was completed by the Assessing Officer on the declared income vide order dated 17-10-1988 passed under Section 143(1).

3. The CIT on a subsequent perusal of the record opined that the order passed by the ITO was erroneous and prejudicial to the interest of revenue on account of the following reasons which were stated in the show-cause notice issued to the assessee :

(a) In para 5 of Schedule 'B' on Notes on accounts, the auditors have observed that 'during the year 35,775 equity shares of Swadeshi Polytex Ltd. held as stock in trade investment were transferred to 'Investment Account' at prevailing market rate, difference in cost and market rate has been transferred to 'Investment Fluctuation Reserve Account'. Thereafter these shares have been contributed as company's capital in M/s. Gayatri & Annapurna, a partnership firm.

(b) In para 6 of the Schedule 'B', it is observed that duringthe year under audit, the company has changed its method of accounting from mercantile to cash basis. If this change has not occurred the profit during the year as per profit and loss account would have been higher by Rs. 1,650.

The above observations which are basically material to the correct computation of income for the year under consideration have not been subjected to even preliminary examination by the Assessing Officer. Therefore, the assessment so framed is erroneous in so far as it is prejudicial to the interest of revenue. In the circumstances, you are hereby given an opportunity to show cause as to why the assessment may not be set aside.

4. Inresponse to the show-cause notice, it was stated that the observation in the Notes to the Accounts referred to in the notice under Section 263 were available with the Assessing Officer and it was only after scrutinizing these and applying his mind that he said officer had completed the assessment under Section 143(1) of the Act. Further it was contended that the aforesaid observations had no material bearing to any income having escaped assessment or it come being wrongly computed since the law permitted conversion of stock in trade into investment and no profit or gain arising on account of revaluation during such conversion. Another argument which was advanced was that the subsequent contribution of the shares to a partnership firm as capital contribution also

did not give rise to any taxable income. Attention was also invited to the provisions of Section 45(3), which were inserted w.e.f. 1-4-1988 subjecting to tax such transactions, but which was not applicable to the assessment year under consideration. As regards the change in the method of accounting from mercantile to cash. it was stated that the relevant facts were duly disclosed in the balance sheet and furthermore no permission was required from the Assessing Officer for the aforesaid change. The further argument advanced in this connection was that no income had escaped tax as a result of the aforesaid change. In summing up the arguments, it was contended that the order passed by the ITO, neither being erroneous nor prejudicial to the interest of revenue, the proceedings under Section 263 be dropped.

5. The CIT was, however, not convinced with the aforesaid arguments and observed that although the relevant information had been given in the audited accounts, the Assessing Officer did not apply his mind and did not make use of such information. A reference was also made to the no availability of the records of the partnership firm with the Assessing Officer which could have indicated "that the assessee had resorted to tax planning". According to the CIT, the Assessing Officer was supposed to examine the issue in the light of the decision of the Hon'ble Supreme Court in the case of McDowell & Co. Ltd. v. CTO [1985] 154 ITR 148'.

6. As regards the change in the method of accounting, the CIT accepted the proposition that an assessee was entitled to effect a change but was also of the view that the Assessing Officer should be satisfied that the change was bona fide.

7. The CIT, thereafter, set aside the assessment order and directed the Assessing Officer to reframe it after looking into the aforesaid aspects. In doing so, the CIT observed as under :

On a careful consideration of the facts and circumstances of the case and in view of the foregoing discussion, I hold that as the Assessing Officer has failed to make even basic enquiries about the precise nature of transaction relating to 35,775 shares and the consequences flowing from it and has also failed to look into the aspect relating to change in the method of accounting, the assessment order under Section 143(1) dated 17-10-1988 is erroneous in so far as it is prejudicial to the interest of revenue. Therefore, in exercise of the powers conferred upon me under Section 263 of the Income-tax Act, 1961, I would set aside the assessment with the directions that the same may be made afresh after looking into the above referred two aspects.

8. The learned counsel for the appellant at the outset contended that in the case of an assessment completed under Section 143(1), no detailed investigation was required on the part of the ITO and all that was required to be done, was to follow the executive instructions pertaining to the completion of assessments under the said section. According to the learned counsel, certain types of adjustments could be made by the ITO and in case there was an improper adjustment, then resort could be made by an assessee to the provisions of Section 143(2)(a) and by the ITO to Sub-clause (b) of the said section. It was further argued that in case the assessment completed under Section 143(1) were interfered with by the CIT under Section 263, then the provisions of Section 143(2)(a) and (b) would become absolutely redundant.

9. On the merits of the case, the learned counsel advanced the following arguments :

(a) That conversion of stock-in-trade into investment did not give rise to any taxable event.

(b) The conversion at market rate and crediting the difference to the 'Investment Fluctuation Reserve Account' also did not give rise to any taxable event.

(c) The action on the part of the assessee in contributing shares to a partnership firm towards capital although constituting a 'transfer' did not result in any taxable income, inasmuch as no capital gains were exigible in view of the decision of the Hon'ble Supreme Court in the case of Sunil Siddharthbhai v. CIT[1985] 156 ITR 5092. The amendment in the law by the introduction of Section 45(3) came about w.e.f. from 1-4-1988 and was not applicable to the assessment year under appeal.

(d) That the change in the method of accounting did not have any substantial tax effect and the department itself had accepted the same in the subsequent years.

10. In summing up his arguments, the learned counsel contended that the order passed by the ITO was neither erroneous nor prejudicial to the interest of the revenue, inasmuch as the points raised by the CIT did not have any effect on the taxable income. It was, therefore, urged that the order passed under Section 263 be quashed.

11. The learned Departmental Representative, on the other hand, supported the order passed by the CIT under Section 263, as, according to him, the ITO, while framing the assessment under Section 143(1) had not applied his mind and in the process overlooked certain important aspects having a bearing on the case. According to him, an order under Section 143(1) could also be interfered with by the CIT in exercise of his revisionary powers under Section 263.

12. In support of the aforesaid arguments, the Departmental Representative placed reliance on the following decisions :

1. CIT v. Smt Bibi Zaibunnisa [1990] 185 ITR 2843 (Pat.).

2. CIT v. Vithal Textiles [1989] 175 ITR 629 (MP).

3. Addl. CIT v. Mukur Corpn. [1978] 111 ITR 312 (Guj.).

13. On the merits of the case, namely, the conversion of stock-in-trade into investments, contribution of shares as capital to a firm and the change in the system of accounting, the learned Departmental Representative reiterated the reasons recorded by the CIT in invoking the provisions of Section 263.

14. In his short reply, the learned counsel for the appellant stated that this was a case where an enquiry not of facts but of law arising from a decision of Supreme Court had been directed and this could never be the subject-matter of action under Section 263. As regards the decisions relied upon

by the learned Departmental Representative, it was contended that these were distinguishable on facts and not at all applicable.

15. In ITA No. 3071 (Del.)/91, the facts leading to the initiation of proceedings-under Section 263 are more or less the same except that the assessment year involved is 1986-87 and the return was filed declaring a loss of Rs. 4,990 and which was accepted vide order dated 18-11-1988 under Section 143(1). Furthermore, there was no change in the method of accounting. The order passed by the CIT was also on the same lines and both the parties have contended that the arguments advanced by them in the earlier appeal be incorporated in the present appeal as well.

16. I have examined the rival submissions and have also perused the separate orders passed by the CIT under Section 263. The decisions cited at the bar have also been duly considered. In my opinion, the powers under Section 263 on the facts and in the circumstances of the case, were not validly initiated. It is not the case of the revenue that the assessments completed under Section 143(1) were in violation of any executive instructions or they transgressed the relevant provisions of the Act. It is also not the case of the revenue that these assessments were wrongly completed under Section 143(1) whereas they were supposed to be scrutiny assessments. A perusal of the audited accounts which were filed along with the returns shows that the subject-matter of the show-cause notice under Section 263 and the subsequent discussion in the orders itself has been picked up from these audited accounts. Nobody can say that the relevant facts were not disclosed by the assessee and it can safely be assumed that these were gone into by the ITO before framing assessments under Section 143(1). In case it is assumed that he did not go through these notes, then my opinion is that he was not required to do so, inasmuch as what has to be looked into, has been specifically mentioned in the executive instructions issued from time to time to the Assessing Officers. It is also not the case of the revenue that the adjustments specifically provided in the relevant section had not been made. That apart, the Assessing Officer could have resorted to the provisions of Section 143(2)(b) if any thing was found lacking subsequently but which he did not do. As rightly contended by the learned counsel, no sanctity could be attached to an assessment completed under Section 143(1) by following executive instructions in case the same was to be tampered with, under Section 263 by the CIT. I am also of the opinion that the revisionary powers under Section 263 cannot be invoked only with a view to directing the ITO to reframe an already completed assessment by making fishing enquiries. The CIT in his orders has referred to the decision of the Hon'ble Supreme Court in the case of McDowell & Co. Ltd. (supra) referring in this connection to a tax planning device' having been resorted to by the assessee. This, according to me, is purely on surmises and conjectures and as rightly pointed out by the learned counsel, there is ultimately no tax effect in respect of any of the transactions referred to by the CIT. The Hon'ble Supreme Court in the case of Sunil Siddharthbhai (supra) has clearly held that contribution of assets as capital in a firm does not result in taxable capital gains in the absence of a 'consideration' although it constitutes a 'transfer'. In case the issue before me is viewed in the light of the aforesaid decision, then no capital gains are attracted and in case the transaction is to be treated as non-genuine or bogus, then the net result would be that the act of contributing the shares as capital in the firm is presumed not to have taken place at all. This is the view expressed by their Lordships of the Gujarat High Court in the case of CIT v. Harikishan Jethalal Patel [1987] 33 Taxman 217. It is only with effect from 1-4-1988 that such a transaction has been brought into the tax net by the introduction of Section 45(3) of the

Income-tax Act, 1961. Then again, there is a statement at the bar by the learned counsel of the assessee that the change in the method of accounting has been duly accepted in the subsequent assessment years.

17. As regards the decisions relied upon by the learned Departmental Representative, I am of the view that these are distinguishable and not applicable to the facts which have been raised before me in these appeals. In the case of Mukur Corpn.'s case (supra), the assessment was one framed under Section 143(3) and it was on the facts prevailing in that case that their Lordships of the Gujarat High Court held that the revision by the CIT was proper and justified. The point in the case of Vithal Textiles (supra) was whether the CIT had jurisdiction to revise an order passed by the ITO in accordance with the directions given by the IAC under Section 144B. The matter before the Hon'ble Patna High Court pertained to a "special" scheme of assessment under Section 143(1) and it was on the facts of that case that action under Section 263 was approved. This was also the position in another decision delivered by the Hon"ble Patna High Court in the case of CIT v. Pushpa Devi [1987] 164 ITR 6394.

18. Before I part with these appeals, I would only like to refer to a circular issued by the Directorate of Inspection (FT and Audit), New Delhi, which reads as follows :

This Directorate had received several references from different Commissioners seeking guidance as to whether remedial action under Section 263 could be taken in cases completed under 'Summary Assessment Scheme' where glaring and apparent mistakes in computation of income have been detected resulting in substantial loss of revenue. For instance, CIT Poona had cited a case where partnership firm had claimed a wrong deduction of Rs. 2.34 lacs in respect of medical expenses on the treatment of a partner. In another case a totally incorrect deduction in respect of investment allowance was claimed by a firm and allowed under Section 143(1). On a reference made by the Directorate to the Board seeking clarification as to whether provision of Section 263 should be invoked in such cases, the Member (R & A) has observed as under:

No remedial action is necessary in summary assessment cases, as the revenue loss if any is consciously suffered by the Govt. to utilise resources for scrutiny and investigations of larger cases. In such cases CIT should only inform Audit that the cases are completed under the Summary Assessment Scheme.

The above observations of the Member (R & A) reflect the views of the Board on the subject and are being brought to the notice of all the Commissioners of Income-tax for their information and guidance.

[F. No. RAI/86-87/DIT dated 26-8-1987 from D.I. (IT & Audit), New Delhi].

19. The aforesaid circular, although issued by the Directorate of Inspection, reflects the view of the CBDT as mentioned therein. I am not going to venture to pronounce whether the aforesaid circular is binding or not, but all that I would like to say is that it reflects the views of the tax administration vis-a-vis the assessments completed under Section 143(1).

20. In the final analysis, I quash the orders passed by the CIT under Section 263 in both the cases.

21. The appeals are allowed.