

S. NARAYANAPPA & ORS.

v.

COMMISSIONER OF INCOME-TAX, BANGALORE.

September 27, 1966

[J. C. SHAH, V. RAMASWAMI AND V. BHARGAVA. JJ.]

*Income-tax Act (11 of 1922), s. 34—Scope of.*

For the assessment year 1951-52, the appellant did not file a return of his income under s. 22 of the Income-tax Act, 1922, but the Income-tax Officer assessed the income at a certain figure. When examining the material for the assessment year 1955-56, it was discovered that the assessee made large investments and suppressed items of house property acquired by him. The Income-tax Officer, therefore, issued a notice under s. 34(1) and after examining the return assessed the income for the assessment year 1951-52 at a much higher figure. In the reference to the High Court, the appellant questioned the jurisdiction of the Officer to initiate proceedings under s. 34(1), but the High Court held against him.

In appeal to this Court,

HELD: (i) The Income-tax Officer had reasonable grounds for thinking that there was non-disclosure of material facts on the part of the appellant and that there was under-assessment for the assessment year 1951-52, caused by the assessee's failure to submit his return. [593 C]

Two conditions must be satisfied in order to confer jurisdiction on the Income-tax Officer to issue notice under s. 34, namely, (i) the Officer must have reason to believe that the income, profits or gains chargeable to income-tax had been under-assessed; (ii) he must have reason to believe that such under-assessment had occurred by reason of the omission or failure on the part of the assessee to make a return or disclose fully all material facts necessary for assessment. The existence of the belief, and whether the reasons for the belief have a rational connection with or relevant bearing on, the formation of the belief, are open to examination by the court. But if there are in fact some reasonable grounds for the Officer to believe that there had been a non-disclosure as regards any fact, which could have a material bearing on the question of under-assessment, that would be sufficient to give him jurisdiction to issue the notice under s. 34, and their sufficiency cannot be challenged by the assessee. [592 C-H]

(ii) The scheme of s. 34 is that if the conditions of the main section are satisfied a notice has to be issued to the assessee. But before issuing the notice the proviso requires that the officer should record his reasons and obtain the sanction of the Commissioner for initiating action under the section. But there is no requirement in the Act that the reasons which induced the Commissioner to accord sanction should also be communicated to the assessee. [593 F-G]

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 562 of 1965.

Appeal by special leave from the judgment and order dated July 24, 1963 of the Mysore High Court in I.T.R.C. No. 3 of 1963.

**A** *R. Gopalakrishnan*, for the appellants.

*S. V. Gupte*, Solicitor-General, *N. D. Karkhanis* and *R. N. Sachthey*, for the respondent.

The Judgment of the Court was delivered by

**B** **Ramaswami J.** The appellant was carrying on business in jewellery, copper-wire and money lending. The books of accounts of the appellant were closed on the 30th of June every year. For the assessment year 1951-52 (for which the previous year ended on 30th June, 1950) the appellant did not comply with the notice issued under s. 22(2) or section 22(4) of the Income-tax Act. No return was filed by the appellant. The assessment was completed by the

**C** Income-tax Officer on such material as was available on the 23rd. February, 1955 and the income was assessed at Rs. 36,068/-. Subsequently, while making assessment for the assessment year 1955-56, the appellant was asked to furnish a wealth statement which was actually filed on the 30th June, 1954. From the wealth statement it was found that the appellant had made investments for Rs. 39,000/-

**D** during the previous year which ended on the 30th June, 1950, though in respect of that previous year, the appellant's income was assessed only at Rs. 36,068/-. A scrutiny of the wealth statement and the Bank account and the extensive nature of the business carried on by the appellant led the Income-tax Officer to entertain a belief that the income of the year 1951-52 had been under-assessed. He

**E** accordingly issued a notice under s. 34(1) and after examining the return made, he assessed the income of the appellant at Rs. 89,002/- by his order dated the 31st March, 1960. The appellant filed an appeal against the assessment order to the Appellate Assistant Commissioner but the appeal was dismissed, the appellant preferred a further appeal to the Income-tax Appellate Tribunal,

**F** Madras Bench. The appellant did not dispute the quantum of the assessment but only the jurisdiction of the Income-tax Officer to initiate proceedings under s. 34(1). The Tribunal by its order dated the 31st January, 1962 over-ruled the objection and dismissed the appeal. At the instance of the appellant, the Tribunal referred the following question of law for the opinion of the High Court:

**G** "Whether the Income-tax Officer had jurisdiction to initiate proceedings for the assessment year 1951-52 under the provisions of s. 34(1) (a) of the Indian Income-tax Act of 1922".

The High Court answered the question against the appellant holding

**H** that the Income-tax Officer had jurisdiction to initiate proceedings against the appellant under s. 34(1) (a) of the Act for the assessment year 1951-52. This appeal is brought by special leave against the judgment of the High Court dated the 24th July, 1963.

On behalf of the appellant Mr. Gopalakrishnan contended in the first place that the reasons which induced the Income-tax Officer to initiate the proceedings under s. 34 were justiciable. It was submitted that those reasons should have been communicated by the Income-tax Officer to the assessee before the assessment was made. In this connection, the further argument of the appellant was that those reasons "must be sufficient for a prudent man to come to the conclusion that the income had escaped assessment". In our opinion, there is no substance in any one of these arguments. It is true that two conditions must be satisfied in order to confer jurisdiction on the Income-tax Officer to issue the notice under s. 34 in respect of assessments beyond the period of four years, but within a period of eight years, from the end of the relevant year. The first condition is that the Income-tax Officer must have reason to believe that the income, profits or gains chargeable to income-tax had been under-assessed. The second condition is that he must have reason to believe that such "under-assessment" had occurred by reason of either (i) omission or failure on the part of an assessee to make a return of his income under s. 22, or (ii) omission or failure on the part of the assessee to disclose fully and truly all the material facts necessary for his assessment for that year. Both these conditions are conditions precedent to be satisfied before the Income-tax Officer acquires jurisdiction to issue a notice under the section. But the legal position is that if there are in fact some reasonable grounds for the Income-tax Officer to believe that there had been any non-disclosure as regards any fact, which could have a material bearing on the question of under-assessment that would be sufficient to give jurisdiction to the Income-tax Officer to issue the notice under s. 34. Whether these grounds are adequate or not is not a matter for the Court to investigate. In other words, the sufficiency of the grounds which induced the Income-tax Officer to act is not a justiciable issue. It is of course open for the assessee to contend that the Income-tax Officer did not hold the belief that there had been such non-disclosure. In other words, the existence of the belief can be challenged by the assessee but not the sufficiency of the reasons for the belief. Again the expression "reason to believe" in section 34 of the Income-tax Act does not mean a purely subjective satisfaction on the part of the Income-tax Officer.

The belief must be held in good faith: it cannot be merely a pretence. To put it differently it is open to the Court to examine the question whether the reasons for the belief have a rational connection or a relevant bearing to the formation of the belief and are not extraneous or irrelevant to the purpose of the section. To this limited extent, the action of the Income-tax Officer in starting proceedings under s. 34 of the Act is open to challenge in a court

- A of law. [See *Calcutta Discount Co. Ltd., v. Income-tax Officer Companies District I, Calcutta and Anr.*(<sup>1</sup>)]

B In the present case the High Court has pointed out that the Income-tax Officer when examining the relevant material in the proceedings for the assessment year 1955-56 found that the appellant had made investments to the extent of Rs. 39,000/- in the account year under question when the income assessed was only Rs. 36,068/-. On further examination it was discovered that items of house property acquired long before the relevant accounting year had been suppressed. The High Court, therefore, held that the Income-tax Officer had reasonable grounds for thinking that there was non-disclosure on the part of the appellant and that there was under-assessment for the assessment year 1951-52.

D It was also contended for the appellant that the Income-tax Officer should have communicated to him the reasons which led him to initiate the proceedings under s. 34 of the Act. It was stated that a request to this effect was made by the appellant to the Income-tax Officer, but the Income-tax Officer declined to disclose the reasons. In our opinion, the argument of the appellant on this point is misconceived. The proceedings for assessment or re-assessment under s. 34(1) (a) of the Income-tax Act start with the issue of a notice and it is only after the service of the notice that the assessee, whose income is sought to be assessed or re-assessed, becomes a party to those proceedings. The earlier stage of the proceeding for recording the reasons of the Income-tax Officer and for obtaining the sanction of the Commissioner are administrative in character and are not quasi-judicial. The scheme of s. 34 of the Act is that, if the conditions of the main section are satisfied a notice has to be issued to the assessee containing all or any of the requirements which may be included in a notice under sub-section (2) of section 22. But before issuing the notice, the proviso requires that the officer should record his reasons for initiating action under section 34 and obtain the sanction of the Commissioner who must be satisfied that the action under s. 34 was justified. There is no requirement in any of the provisions of the Act or any section laying down as a condition for the initiation of the proceedings that the reasons which induced the Commissioner to accord sanction to proceed under section 34 must also be communicated to the assessee.

H In *The Presidency Talkies Ltd. v. First Additional Income-tax Officer, City Circle II, Madras*,(<sup>2</sup>) the Madras High Court has expressed a similar view and we consider that that view is correct. We accordingly reject the argument of the appellant on this aspect of the case.

(1) 41 I.T.R. 191.

(2) 25 I. T. R. 447.

Lastly, it was submitted by the appellant that the proceedings under s. 34 were invalid because the Income-tax Officer did not entertain the belief that the under-assessment was made by reason of the omission or failure on the part of the assessee to make a return under s. 22 or to disclose fully and truly all material facts necessary for the first assessment. There is no substance in the argument. The Tribunal has found that there was direct connection or nexus between the assessee's omission or failure to make a return and the under-assessment made by the Income-tax Officer for the year 1951-52. The High Court has affirmed this finding and concluded that the proceedings under s. 34(1)(a) of the Act were not defective in law.

For these reasons we dismiss this appeal with costs.

V.P.S.

*Appeal dismissed*