A COMMISSIONER OF INCOME TAX, CHENNAI

v.

M/S. ALAGENDRAN FINANCE LTD.

JULY 27, 2007

B [S.B. SINHA AND HARJIT SINGH BEDI, JJ.]

Income Tax Act, 1961—s. 263—Assessment—Revision by Commissioner—Limitation period—Date of commencement—Commissioner exercising its revisional jurisdiction reopened order of assessment only in relation to 'lease equalization fund', which being not the subject of the reassessment proceedings, period of limitation provided for under s. 263(2) would commence from the date of original assessment order and not from the date of order of reassessment—Doctrine of merger not applicable in a case of this nature.

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D **The Commissioner of Income Tax exercising its revisional jurisdiction in terms of Section 263 of the Income Tax Act, 1961 reopened the order of assessment only in relation to 'lease equalization fund' which was not the subject of the reassessment proceedings.**

In appeal before this Court, the question which arose for consideration E **is whether the period of limitation provided for under Sub-section (2) of Section 263 of the Act would begin to run from the date of the order of assessment and not from the order of reassessment and that the doctrine of merger would not apply in a case of this nature.**

Dismissing the appeal, the Court

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HELD: 1.1. A bare perusal of the order passed by the Commissioner of Income Tax would clearly demonstrate that only that part of order of assessment which related to 'lease equalization fund' was found to be prejudicial to the interest of the Revenue. The proceedings for reassessment have nothing to do with the said head of income. Doctrine of merger, therefore, G **would not apply in a case of this nature. Furthermore, Explanation (c) appended to Sub-section (1) of Section 263 of the Act is clear and unambiguous as in terms thereof doctrine of merger applies only in respect of such items which were the subject matter of appeal. [Paras 7 and 8] [564-A-C]**

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1.2. Once an order of assessment is reopened, the previous underassessment will be held to be set aside and the whole proceedings would start afresh but the same would not mean that even when the subject matter of reassessment is distinct and different, the entire proceeding of assessment would be deemed to have been reopened. It is not a case where the subject matter of reassessment and subject matter of assessment were the same. They were not. [Paras 10 and 12] [565-H; 566-A-B; 567-F-G]

1.3. Keeping in view the facts and circumstances of this case and, in particular, having regard to the fact that the Commissioner of Income Tax exercising its revisional jurisdiction reopened the order of assessment only in relation to lease equalization fund which being not the subject of the reassessment proceedings, the period of limitation provided for under Sub-section (2) of Section 263 of the Act would begin to run from the date of the order of assessment and not from the order of reassessment.

[Para 15] [569-B-D]

Commissioner of Wealth-Tax **v.** *A.K. Thanga Pillai,* **252 ITR 260 and** *Commissioner of Income-Tax* **v.** *Kanubhai Engineers (P.) Ltd.,* **241 ITR 665, approved.**

Commissioner of Income-Tax **v.** *Shri Arbuda Mills Ltd.,* **231 ITR 50, relied on.**

Hind Wire Industries Ltd. **v.** *Commissioner of Income Tax,* **212 ITR 639;** *Commissioner of Income Tax* **v.** *Sun Engineering Works P. Ltd.,* **198 ITR 297 and** *V. Jaganmohan Rao* **v.** *CIT and CEPT,* **75 ITR 373, referred to.**

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 3301 of 2007.

From the Judgment & Order 18.01.2006 of the High Cout of Judicature at Madras in Tax Appeal No. 1384 to 1386 of 2005 and TCMP Nos. 1203-1204 of 2005.

Rajiv Dutta, B.L. Chiber, M.F. Humayunisa, Kumar Dushyant Singh and B.V. Balaram Das for the Appellant.

Anil Diwan, T.N. Seetharaman, Bina Gupta and Shweta Verma for the Respondents.

The Judgment of the Court was delivered by

S.B. SINHA, J. 1. Leave granted.

A 2. Whether for the purpose of computing the period of limitation envisaged under Sub-section (2) of Section 263 of the Income Tax Act, 1961 (for short "the Act"), the date of order of assessment or that of the reassessment, is to be taken into consideration is the question involved in this appeal which arises out of a judgment and order dated 18.01.2006 passed by a Division Bench of the High Court of Judicature at Madras passed in B Income Tax Appeal No. 1384 to 1386 of 2005.

3. The said question arises on the following facts :

Respondent is a company incorporated under the Indian Companies Act, 1956. It filed its returns for assessment under the Act for the assessment C years 1994-95, 1995-96 and 1996-97 on 23.11.1994, 27.11.1995 and 26.11.1997 respectively. Assessment for the year 1994-95 was completed on 27.02.1997 and those of the Assessment Years 1995-96 and 1996-97 were completed on 12.05.1997 and 30.03.1998 respectively. In the said orders of assessment, the assessee's return under the Head 'Lease Equalization Fund' was accepted. D However, proceedings for reassessment were initiated by the assessing officer on 05.03.2004. Orders of reassessment were passed on 28.03.2002. Proceedings for reassessment, however, were initiated only in respect of three items, viz., (i), the expenses claimed for share issue, (ii), bad and doubtful debts and (iii), excess depreciation on gas cylinders and goods containers.

E Although the assessee's return in respect of lease equalization was not the subject matter of the reassessment proceedings, the Commissioner of Income Tax purported to invoke his revisional jurisdiction in terms of Section 263 of the Act and by an order dated 29.03.2004 held as under:

> F "5. In short, from the example given it is the depreciation on the leased assets that is clamed as Book Depreciation and disallowed in the computation of income, the assessee sought to claim in the form of Lease Equalisation from the lease rentals by virtue of the guidelines note of the Institute of Chartered Accountants of India.
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> G *** *** ***
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> 7. Since the assessee has not given the complete details, the method adopted by the assessee in arriving at the correct profit for the corresponding year cannot be checked. I clearly feel that the orders by the Assessing Officer are prejudicial to the interest of the revenue as the lease rentals had not been properly brought to tax. Hence, all

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the three assessments are reopened u/s 263 and the Assessing Officer is directed to check and assess the lease rentals from Lease equalisation fund, if any, and to bring to tax the same for all the above three years."

Pursuant to or in furtherance of the said order, reassessment proceedings were carried out in respect of the aforementioned assessment years by the Assistant Commissioner of Income Tax only in respect of the income on equalization reserve stating:

"I have considered the various arguments of the assessee's representative and I am satisfied that the deduction made from the gross lease rent is only a provisional and not an actual expenditure and therefore the same is to be disallowed and added to the income returned..."

The matter came up for consideration before the Income Tax Appellate Tribunal wherein the contention of the respondent that the said purported proceedings under Section 263 of the Act were barred by limitation, found favour with, opining:

"6. We have carefully gone through the record and considered the rival submissions. In our view, the contentions of the Assessee deserve to succeed. The facts of the case clearly show the claim of lease equalisation fund, if at all accepted, is an error committed by the Assessing Officer in his order passed under Sec. 143(3) of the Act for the Asst. Year 94-95 on 27.2.97, for the Asst. Year 95-96 on 12.5.97 and for the Asst. Year on 30.3.98. The Assessee, no doubt, took up these assessments in appeal before the CIT (Appeals) and thereafter the assessment itself was subject to proceedings under Sec. 148 and ultimately, the orders of reassessment were framed on 28.3.2002. All the subsequent events are in respect of matters other than the allowance of lease equalization fund. In other words, the error, if any, has been committed, it was done in the order of the Assessing Officer passed Asst. the year 97-98. Therefore, these orders very much subsist despite the subsequent proceedings under sec. 148 of the Act."

The learned Tribunal referred to several decisions of this Court and other High Courts for arriving *inter alia* at the following conclusion:

"8. In the light of the above decisions and authorities, we are of the opinion that the impugned order passed under Sec. 263 on 29.03.2004

A are clearly barred by limitation with reference to the orders passed under Sec. 143(3) by the Assessing Officer for the above Asst. years on 27.2.97; 25.12.97 and 30.3.98 respectively. Accordingly, the orders of the CIT under Sec. 263 are vacated and the ground taken by the Assessee is allowed."

B Revenue preferred an appeal thereagainst before the High Court which was dismissed by a Division Bench stating:

"2. Learned Senior Central Government Standing Counsel submits that the very same issue has been raised and decided by the Court against the Revenue in the case of *CWT* v. *A.K. Thanga Pillai,* (252 ITR 260)."

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Aggrieved by and dissatisfied therewith, the Revenue is before us.

4. Mr. Rajiv Dutta, learned senior counsel appearing on behalf of the appellant in support of the appeal *inter alia* would submit that having regard to the Explanation appended to Sub-section (3) of Section 263 of the Act as D also in view of the doctrine of merger, the Tribunal committed a manifest error in passing the impugned judgment insofar as it failed to take into consideration that in law computation of period of limitation was to commence from the date of passing of the order of reassessment viz., 28.03.2002 and not from the date of the initial assessment, and as the proceeding under Section 263 was E initiated on 05.03.2004, the provision of sub-section (2) of Section 263 would not be attracted in the instant case. Strong reliance in this behalf has been placed on *Hind Wire Industries Ltd.* v. *Commissioner of Income Tax,* [212 ITR 639].

5. Mr. Anil Diwan, learned senior counsel appearing on behalf of the F respondent – assessee, on the other hand, submitted:

(i) The income head 'lease equalization fund' being not the subject matter of the reassessment proceedings, the doctrine of merger will have no application in the instant case and in that view of the matter, the impugned order of the Tribunal as also the High G Court is unassailable.

(ii) The issue has rightly been held by the High Court to be squarely covered by the decision of the Madras High Court in *Commissioner of Wealth-Tax* v. *A.K. Thanga Pillai,* [252 ITR 260].

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6. Before embarking upon the rival contentions of the parties raised before us, we may notice the relevant part of Section 263 of the Act which is as under:

"263. *Revision of orders prejudicial to revenue* - (1) The Commissioner may call for and examine the record of any proceeding under this Act, and if he considers that any order passed therein by the Assessing Officer is erroneous in so far as it is prejudicial to the interests of the revenue, he may, after giving the assessee an opportunity of being heard and after making or causing to be made such inquiry as he deems necessary, pass such order thereon as the circumstances of the case justify, including an order enhancing or modifying the assessment, or cancelling the assessment and directing a fresh assessment.

Explanation.-For the removal of doubts, it is hereby declared that, for the purposes of this sub-section,-

(a) *** *** ***

(b) *** *** ***

(c) where any order referred to in this sub-section and passed by the Assessing Officer had been the subject matter of any appeal filed on or before or after the 1st day of June, 1988, the powers of the Commissioner under this sub-section shall extend and shall be deemed always to have extended to such matters as had not been considered and decided in such appeal.

(2) No order shall be made under sub-section (1) after the expiry of two years from the end of the financial year in which the order sought to be revised was passed.

(3) Notwithstanding anything contained in sub-section (2), an order *in revision* under this section may be passed at any time in the case of an order which has been passed in consequence of, or to give effect to, any finding or direction contained in an order of the Appellate Tribunal, the High Court or the Supreme Court.

Explanation.—In computing the period of limitation for the purposes of sub-section (2), the time taken in giving an opportunity to the assessee to be reheard under the proviso to section 129 and any period during which any proceeding under this section is stayed by

A an order or injunction of any court shall be excluded."

7. A bare perusal of the order passed by the Commissioner of Income Tax would clearly demonstrate that only that part of order of assessment which related to lease equalization fund was found to be prejudicial to the interest of the Revenue. The proceedings for reassessment have nothing to B do with the said head of income. Doctrine of merger, therefore, would not apply in a case of this nature.

8. Furthermore, Explanation (c) appended to Sub-section (1) of Section 263 of the Act is clear and unambiguous as in terms thereof doctrine of merger applies only in respect of such items which were the subject matter of appeal C and not which were not. The question came up for consideration before this Court in *Commissioner of Income Tax* v. *Sun Engineering Works P. Ltd.*, 198 ITR 297. Therein the assessee raised a contention that once jurisdiction under Section 147 of the Act is invoked, the whole assessment proceeding became reopened, which was negatived by the court opining:

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> "Section 147, which is subject to Section 148, divides cases of income escaping assessment into two clauses i.e. viz. (a) those due to the non-submission of return of income or non-disclosure of true and full facts and (b) other instances. Explanation (1) defines as to what constitutes escape of assessment. In order to invoke jurisdiction E under Section 147(a) of the Act, the ITO must have reason to believe that some income chargeable to tax of an assessee has escaped assessment by reason of the omission or failure on the part of the assessee either to make a return under Section 139 for the relevant assessment year or to disclose fully and truly material facts necessary for the assessment for that year. Both the conditions must exist before F an ITO can proceed to exercise jurisdiction under Section 147(a) of the Act. Under Section 147(b) the Income-tax Officer also has the jurisdiction to initiate proceedings for reassessment where he has reason to believe, on the basis of information in his possession, that income chargeable to tax has been either under-assessed or has been G assessed at too low a rate or has been made the subject of excessive relief under the Act or excessive loss or depreciation allowance has been computed. In either case whether the Income-tax Officer invokes his jurisdiction under Clause (a) or Clause (b) or both, the proceedings for bringing to tax an 'escaped assessment' can only commence by issuance of a notice under Section 148 of the Act within the time

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prescribed under the Act. Thus, under Section 147, the assessing officer has been vested with the power to "assess or reassess" the escaped income of an assessee. The use of the expression "assess or reassess such income or recompute the loss or depreciation allowance" in Section 147 after the conditions for reassessment are satisfied, is only relatable to the preceding expression in Clauses (a) and (b) viz., "escaped assessment". The term "escaped assessment" includes both "non-assessment" as well as "under assessment". Income is said to have "escaped assessment" within the meaning of this section when it has not been charged in the hands of an assessee in the relevant year of assessment. The expression "assess" refers to a situation where the assessment of the assessee for a particular year is, for the first time, made by resorting to the provisions of Section 147 because the assessment had not been made in the regular manner under the Act. The expression "reassess" refers to a situation where an assessment has already been made but the Income-tax Officer has, on the basis of information in his possession, reason to believe that there has been under assessment on account of the existence of any of the grounds contemplated by the provisions of Section 147(b) read with the Explanation (I) thereto."

9. We may at this juncture also notice the decision of this Court in *Hind Wire Industries Ltd* (supra) wherein the decision of this Court in *V. Jaganmohan Rao* v. *CIT and CEPT,* [75 ITR 373] interpreting the provisions of Section 34 of the Act was reproduced which reads as under:

"Section 34 in terms states that once the Income-tax officer decides to reopen the assessment, he could do so within the period prescribed by serving on the person liable to pay tax a notice containing all or any of the requirements which may be included in a notice under section 22(2) and may proceed to assess or reassess such income, profits or gains. It is, therefore, manifest that once assessment is reopened by issuing a notice under sub-section (2) of section 22, the previous underassessment is set aside and the whole assessment proceedings start afresh. When once valid proceedings are started under section 34(1)(b), the Income-tax Officer had not only the jurisdiction, but it was his duty to levy tax on the entire income that had escaped assessment during that year."

10. There may not be any doubt or dispute that once an order of assessment is reopened, the previous underassessment will be held to be set

A aside and the whole proceedings would start afresh but the same would not mean that even when the subject matter of reassessment is distinct and different, the entire proceeding of assessment would be deemed to have been reopened.

B 11. In *Sun Engineering Works P. Ltd* (supra) also, *V. Jaganmohan Rao,* (supra) was noticed stating:

> "The principle laid down by this Court in *Jaganmohan Rao's* case, therefore, is only to the extent that once an assessment is validly reopened by issuance of a notice under Section 22(2) of the 1922 Act (corresponding to Section 148 of the Act) the previous under C assessment is set aside and the ITO has the jurisdiction and duty to levy tax on the entire income that had escaped assessment during the previous year...The judgment in *Jaganmohan Rao's* case, therefore, cannot be read to imply as laying down that in the reassessment proceedings validly initiated, the assessee can seek reopening of the D whole assessment and claim credit in respect of items finally concluded in the original assessment. The assessee cannot claim recomputation of the income or redoing of an assessment and be allowed a claim which he either failed to make or which was otherwise rejected at the time of original assessment which has since acquired finality. Of course, in the reassessment proceedings it is open to an assessee to E show that the income alleged to have escaped assessment has in truth and in fact not escaped assessment but that the same had been shown under some inappropriate head in the original return, but to read the judgment in *Jaganmohan Rao's* case, as if laying down that reassessment wipes out the original assessment and that reassessment F is not only confined to "escaped assessment" or "under assessment" but to the entire assessment for the year and starts the assessment proceeding *de novo* giving the right to an assessee to reagitate matters which he had lost during the original assessment proceeding, which had acquired finality, is not only erroneous but also against the phraseology of Section 147 of the Act and the object of reassessment G proceedings. Such an interpretation would be reading that judgment totally out of context in which the questions arose for decision in that case. It is neither desirable nor permissible to pick out a word or a sentence from the judgment of this Court, divorced from the context of the question under consideration and treat it to be the complete H 'law' declared by this Court. The judgment must be read as a whole

and the observations from the judgment have to be considered in the light of the questions which were before this Court. A decision of this Court takes its colour from the questions involved in the case in which it is rendered and while applying the decision to a later case, the courts must carefully try to ascertain the true principle laid down by the decision of this Court and not to pick out words or sentences from the judgment, divorced from the context of the questions under consideration by this Court, to support their reasonings..."

It was furthermore held:

"As a result of the aforesaid discussion, we find that in proceedings under Section 147 of the Act, the Income Tax Officer may bring to charge items of income which had escaped assessment other than or in addition to that item or items which have led to the issuance of notice under Section 148 and where ressessment is made under Section 147 in respect of income which has escaped tax, the Income Tax Officer's jurisdiction is confined to only such income which has escaped tax or has been under-assessed and does not extend to revising, reopening or reconsidering the whole assessment or permitting the assessee to reagitate questions which had been decided in the original assessment proceedings. It is only the under-assessment which is set aside and not the entire assessment when reassessment proceedings are initiated. The Income Tax Officer cannot make an order of reassessment inconsistent with the original order of assessment in respect of metters which are not the subject-matter of proceedings under Section 147..."

12. We may at this juncture also take note of the fact that even the Tribunal found that all the subsequent events were in respect of the matters other than the allowance of 'lease equalization fund'. The said finding of fact is binding on us. Doctrine of merger, therefore, in the fact situation obtaining herein cannot be said to have any application whatsoever. It is not a case where the subject matter of reassessment and subject matter of assessment were the same. They were not.

13. It may be of some interest to notice that a similar contention raised at the instance of an assessee was rejected by a 3-Judge Bench of this Court in *Commissioner of Income-Tax* v. *Shri Arbuda Mills Ltd.*, [231 ITR 50]. This Court took note of the amendment made in Section 263 of the Act by the Finance Act, 1989 with retrospective effect from June 1, 1988, inserting

A Explanation (c) to Sub-section (1) of Section 263 of the Act stating:

> "The consequence of the said amendment made with retrospective effect is that the powers under section 263 of the Commissioner shall extend and shall be deemed always to have extended to such matters as had not been considered and decided in an appeal. Accordingly, even in respect of the aforesaid three items, the powers of the Commissioner under section 263 shall extend and shall be deemed always to have extended to them because the same had not been considered and decided in the appeal filed by the assessee. This is sufficient to answer the question which has been referred."

C We, therefore, are clearly of the opinion that in a case of this nature, the doctrine of merger will have no application.

14. The Madras High Court in *A.K. Thanga Pillai* (supra), in our opinion, has rightly considered the matter albeit under Section 17 of the Wealth Tax Act, 1957 which is in *pari materia* with the provisions of the Act. Relying on *Sun Engineering Works P. Ltd* (supra), it was held:

> "Under section 17 of the Wealth-tax Act, 1957, even as it is under section 147 of the Income-tax Act, proceedings for reassessment can be initiated when what is assessable to tax has escaped assessment for any assessment year. The power to deal with underassessment and the scope of reassessment proceedings as explained by the Supreme Court in the case of *Sun Engineering* [1992] 198 ITR 297, is in relation to that which has escaped assessment, and does not extend to reopening the entire assessment for the purpose of redoing the same *de novo*. An assessee cannot agitate in any such reassessment proceedings matters forming part of the original assessment which are not required to be dealt with for the purpose of levying tax on that which had escaped tax earlier. Cases of underassessment are also treated as instances of escaped assessment.
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> The order of reassessment is one which deals with the assessment already made in respect of items which are not required to be reopened, as also matters which are required to be dealt with in order to bring what had escaped in the earlier order of assessment, to assessment. An assessee who has failed to file an appeal against the original order of assessment cannot utilise the reassessment proceedings as an occasion for seeking revision or review of what had been assessed

earlier. He may only question the extent of the reassessment in so far as the escaped assessment is concerned. A

The Revenue is similarly bound..."

The same principle was reiterated by a Division Bench of the Calcutta High Court in *Commissioner of Income-Tax* v. *Kanubhai Engineers (P.) Ltd.*, [241 ITR 665]. B

15. We, therefore, are clearly of the opinion that keeping in view the facts and circumstances of this case and, in particular, having regard to the fact that the Commissioner of Income Tax exercising its revisional jurisdiction reopened the order of assessment only in relation to lease equalization fund C which being not the subject of the reassessment proceedings, the period of limitation provided for under Sub-section (2) of Section 263 of the Act would begin to run from the date of the order of assessment and not from the order of reassessment. The revisional jurisdiction having, thus, been invoked by the Commissioner of Income Tax beyond the period of limitation, it was wholly without jurisdiction rendering the entire proceeding a nullity. D

16. The Tribunal and the High Court, therefore, in our opinion were correct in passing the impugned judgment. The appeal, therefore, being devoid of any merit is dismissed with costs. Counsel's fee assessed at Rs. 25,000/-. E

B.B.B. Appeal dismissed.