

IN THE HIGH COURT OF GUJARAT AT AHMEDABAD
SPECIAL CIVIL APPLICATION No. 2385 of 2001

For Approval and Signature:

HONOURABLE MR.JUSTICE AKIL KURESHI
HONOURABLE MS.JUSTICE HARSHA DEVANI

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- 1 Whether Reporters of Local Papers may be allowed to see the judgment ?
- 2 To be referred to the Reporter or not ?
- 3 Whether their Lordships wish to see the fair copy of the judgment ?
- 4 Whether this case involves a substantial question of law as to the interpretation of the constitution of India, 1950 or any order made thereunder ?
- 5 Whether it is to be circulated to the civil judge ?
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ARVIND POLYCOT LTD. NOW MERGED WITH ARVIND PRODUCTS LTD. -
Petitioner(s)
Versus
CHANDRA RAM OR HIS SUCCESSOR IN OFFICE - Respondent(s)

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Appearance :

MR SN SOPARKAR for Petitioner(s) : 1,
NOTICE SERVED BY DS for Respondent(s) : 1,
MRS MAUNA M BHATT for Respondent(s) : 1,

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CORAM : HONOURABLE MR.JUSTICE AKIL KURESHI

and

HONOURABLE MS.JUSTICE HARSHA DEVANI

Date : 27/08/2012

ORAL JUDGMENT**(Per : HONOURABLE MR.JUSTICE AKIL KURESHI)**

1) The petitioner has challenged a notice dated 15.3.2001 issued by the respondent-Assessing Officer under section 148 of the Income-tax Act, 1961 (hereinafter to be referred to as "the Act") seeking to reopen the assessment in case of the petitioner for the assessment year 1997-98. The petition arises in the following factual background:

1.1) The petitioner is a company registered under the Companies Act, 1956 and is regularly assessed to tax. For the assessment year 1997-98, the petitioner filed its return of income on 25.11.1997 declaring total income of Rs.1,14,26,121/-. The return was taken in scrutiny by the Assessing Officer. He framed assessment under section 143(3) of the Act on 28.3.2000 at total income of Rs.7,15,25,010/-.

1.2) It is this assessment which the Assessing Officer desired to reopen, for which impugned notice dated 15.3.2001 came to be issued. At the request of the petitioner, the Assessing Officer supplied the reasons recorded by him for reopening the assessment. Such reasons read as under:

"In this case, assessment u/s.143(3) was completed on 28.3.2000 determining total income of Rs.7,15,25,008/-. During the appeal proceedings for A.Y. 1995-96, it has come to the notice that the assessee has made payment of Rs.187.54 lacs towards Voluntary Retired Scheme in F.Y.1996-97 relevant to A.Y.1997-98 which was

allowed as revenue expenditure. Now, the CBDT has issued a Circular dated 23.1.2001 in which it has stated that any ex-gratia amount which results in an enduring benefit to assessee should be treated as capital expenditure. In view of this, the said VRS payment is required to be disallowed as capital expenditure. I have therefore, reason to believe that the amount of Rs.187.54 lacs chargeable to tax has escaped assessment. Therefore, notice u/s.148 is issued for A.Y.1997-98.

1.3) At that stage, the petitioner approached this Court challenging the very notice for reopening the assessment.

2) Taking us through the documents on record, Mr. S.N. Soparkar, learned counsel for the petitioner contended that in the original assessment, the Assessing Officer had examined the question of deduction of the payment made by the assessee-Company by way of retrenchment compensation pursuant to Voluntary Retirement Scheme(hereinafter to be referred to as "V.R.S."). The assessee had given detailed reply and supported such a claim placing reliance on several decisions of various Courts. Satisfied that such claim was valid, the Assessing Officer, in the original assessment, made no disallowance. The counsel submitted that the Assessing Officer, having formed an

opinion that the claim was genuine and valid, cannot now reopen the assessment which would be based on mere change of opinion.

3) The counsel further submitted that even otherwise the reasons recorded by the Assessing Officer would not be sufficient for the Assessing Officer to assume jurisdiction to reopen the assessment. As per the Assessing Officer, in view of the circular of Central Board of Direct Taxes (hereinafter to be referred to as "C.B.D.T") such expenditure had to be treated as capital in nature. He therefore, held a belief that income chargeable to tax had escaped assessment. Drawing our attention to the circular of C.B.D.T in question, counsel submitted that in the circular, no specific directions have been issued to treat a particular expenditure as a capital expenditure. In any case, such directions if at all read into circular of the C.B.D.T, would be outside the purview of C.B.D.T under section 119 of the Act. It was further contended that several courts have opined that such expenditure would be revenue expenditure, having been expended wholly and exclusively for the purpose of business. The C.B.D.T.'s circular is contrary to such

settled legal position.

4) The counsel further submitted that in any case reopening of an assessment on the basis of opinion of the C.B.D.T would not be permissible. He submitted that the C.B.D.T cannot give any directives to the Assessing Officer to frame assessment in a particular manner. Further, the opinion of the C.B.D.T cannot be placed on the same footing as that of statutory provisions or the pronouncement by a Court of competent jurisdiction.

5) In support of his contentions, counsel relied on the following decisions:

5.1) In the case of ***Indian and Eastern Newspaper Society Vs. Commissioner of Income-tax, New Delhi***, 119 ITR 996, wherein the Apex Court held and observed that opinion of internal audit party on a point of law would not amount to information enabling the Assessing Officer to form a belief that income chargeable to tax had escaped assessment.

5.2) In the case of ***Sassoon J. David and Co. P. Ltd.***

Vs. Commissioner of Income-tax, Bombay, 118 ITR 261, wherein the Apex Court upheld the assessee's contention that the compensation paid by the assessee-Company to its directors and employees for termination of their services could be stated to have been expended wholly and exclusively for the purpose of the business. The fact that such expenditure was incurred voluntarily and without any necessity would be of no consequence.

5.3) In the case of ***Assistant Commissioner of Income-tax Vs. Dhariya Construction Co., 328 ITR 515,*** wherein the Apex Court observed that the opinion of DVO per se is not an information for the purpose of reopening assessment under section 147 of the Act. The Assessing Officer has to apply his mind to the information, if any, collected and must form a belief thereon.

5.4) Our attention was drawn to the decision of the Calcutta High Court in the case of ***Bhartia Industries Ltd. Vs. Commissioner of Income-tax, Central-III, (2011) 201 Taxman 180.*** In such a decision, the validity of the same C.B.D.T circular dated 23rd

January 2001 came to be examined by the Calcutta High Court in which it was held that the circular would be opposed to the decisions of Calcutta High Court in the case of **Grindlays Bank P.L.C. Vs. C.I.T.**, (1993) 201 ITR 148, **C.I.T Vs. Machinery Mfg. Corpn. Ltd.**, (1992) 198 ITR 559 and in the case of **C.I.T. Vs. Bhor Industries Ltd.**, (2003) 264 ITR 180 (Bombay) and in the case of **C.I.T Vs. O.E.N. India Ltd.**, (2011) 196 Taxman 131 (Kerala). The Court held that the board could not have issued such a circular. In the said judgment the Court referred to and relied upon the decision of the Apex Court in the case of **UCO Bank Ltd. Vs. C.I.T.**, (1999) 104 Taxman 547 (SC), in the case of **Collector of Central Excise Vs. Dhiren Chemical Industries**, AIR 2002 SC 453 and Commissioner of Customs Vs. Indian Oil Corp., (2004) 3 SCC 488 on the question of binding effect of the circular of the board issued under section 119 of the Act.

6) On the other hand, learned counsel Mr. Bhatt for the Revenue opposed the petition contending that the Assessing Officer was within his rights to reopen the assessment. He submitted that the circular of the board would form the source of information, on the

basis of which, the Assessing Officer could form a belief that income chargeable to tax had escaped assessment. He submitted that sufficiency of reasons cannot be gone into by this Court while examining the validity of the notice for reopening the assessment.

7) Heavy reliance was placed on the decision of the Apex Court in the case of **A.L.A. Firm Vs. Commissioner of Income-tax**, 189 ITR 285, wherein the Apex Court had the occasion to examine the validity of the notice for reopening issued by the Assessing Officer on the basis of the decision of the jurisdictional Court, which though existed at the time when the Assessing Officer framed the original assessment, was not noticed by him. In this context, the Apex Court upheld the notice for reopening relying on proposition Nos.(2) and (4) laid down by the Apex Court in the case of **Kalyanji Mavji and Co. Vs. C.I.T**, 102 ITR 287 (SC) to the effect that where in the original assessment the income liable to tax has escaped assessment due to oversight, inadvertence or a mistake committed by the Assessing Officer and where the information may be obtained even from the record of the original assessment from the investigation of

the material on the record, or the facts disclosed thereby or from other enquiry or research into facts or law.

8) Having thus heard learned counsel for the parties and having perused the documents on record, we may recall that in the present case notice for reopening has been issued within four years from the end of relevant assessment year. The additional requirement therefore, that income chargeable to tax had escaped assessment due to the failure on the part of the assessee to disclose fully all material facts, before the assessee the Assessing Officer could assume jurisdiction to reopen the assessment, need not be satisfied. However, the question is whether the Assessing Officer could be said to have some tangible material to hold a belief that income chargeable to tax had escaped assessment. In this context, the question may arise whether the present circular of C.B.D.T could be stated to be a tangible material, on the basis of which, the Assessing Officer could form a belief that income chargeable to tax had escaped assessment.

9) Before taking note of the contents of the C.B.D.T circular in question, let us first examine in some detail, the material before the Assessing Officer and his consideration thereof at the time of original assessment. The assessee claimed deduction of a sum of Rs.187.54 lacs, having spent the same wholly and exclusively for the purpose of business. The Assessing Officer desired to examine such a claim for which he raised a query in his communication dated 8.2.200 as under:

“details of retrenchment compensation and why these should not be disallowed as per last year”

10) In response to such a query, the assessee gave a detailed explanation with respect to the nature of expenditure, why the same should be allowed as revenue expenditure and decisions in support of such a stand. The assessee stated as under:

“You have asked us to show cause why the expenditure incurred on retrenchment compensation should not be disallowed on the basis of assessment order for Asstt. Year 1996-97. In this regard we have to state as under:

Arvind Polycot Limited is in the business of mfg. & sale of textiles. As is already on record, the company is restructuring its business activities.

The Voluntary Retirement Scheme was introduced to streamline the business activities. In this process it has incurred an expenditure of Rs.187.54 lakhs on account of Voluntary Retirement Scheme.

While stating that the amount spent on Voluntary Retirement Scheme is admissible revenue expenditure, we rely on the decision of Madras High Court in case of CIT V. George Oaks Ltd. (197 ITR 288) in which has held as under:

"Held, that the purpose of retrenching the nine workmen as found by the Tribunal was only to contain the loss, reorganise the branch by reducing the staff and to bring about a reduction in the wage bill as well. These were the matters of management pertaining to business consideration and expediency and the expenditure incurred by the assessee in this regard was for purpose of business and also with a view to maintain good relationship with the labour and that expenditure had to be considered as having been laid out wholly and exclusively for business purpose of the assessee. It was therefore deductible."(page 288-289)

We also rely on the following later cases:

CIT V. Ramvilas Services Ltd. (211 ITR 763) (Mds.)

CIT V. Simpson & Co. (No.2) (230 ITR 794) (Mds.)

In case of the Assessee Company it is reorganisation of business of the company by rationalising the labour to reduce the wage bill and this was done for the purpose of carrying on business of manufacture and marketing of textile. It was business consideration and expediency that required reorganisation of existing business in order to survive and make the business profitable in future.

From the Director's Report you would note that the company has as a part of its long term business strategy purchased a textile unit, namely Ankur Textile from Arvind Mills Limited.

They have restructured the production facilities to upgrade its voile production by improving quality and established a marketing net work after acquiring the above unit. This has enabled it to get better quality product and introduce new products. On this account, the relalisation per meter has also gone up. This proves that due to retrenchment the business was never discontinued but on account of changed strategies the Assessee Company has been able to make more profits.

We therefore contend that out claim for deduction of payments made on retrenchment under Voluntary Retirement Scheme is revenue deductible as it is wholly incurred as textile manufacture for continuing in the business of textile. Our claim rightly falls under section 28/37 of the Act and is not a capital expenditure. It will not be out of place to invite your attention to turn over of textile business in this year and subsequent year which is as under:

A.Y. 1997-98

Items	Quantity		Rupees(In Lakhs)
Cloth	69,38,744	Meters	3,081.20
Yarn	35,047	Kgs.	53.08
Waste	2,13,213	Kgs.	51.93

A.Y. 1998-99

Items	Quantity		Rupees (In lakhs)
Cloth	1,13,35,801	Meters	5089.85
Yarn	86,780	Kg.	152.60
Waste	2,78,290	Kg.	70.84

Summing up it is submitted as under:

a. The payment of retrenchment compensation is claimed under section 28/37 of the Act under the head "Profits & Gains of Business".

b. The business prior to the retrenchment was of manufacture & sale of textile and its marketing and that it not only continued but has grown as figures of turn over given above proves it.

c. All the decisions of Madras High Court quoted above cover the claim of the Assessee Company.

d. Expenditure was made wholly and exclusively for the purpose of business as textile manufacturer in order to survive the compensation.

e. The principles of commercial expediency and the test of commercial expediency which justify the action of the assessee company."

11) After eliciting explanation of the assessee on the question of deduction, the Assessing Officer in the original order of assessment, made no disallowances. Under the circumstances, it can be gathered that the Assessing Officer, being fully satisfied with respect to the assessee's claim for deduction, allowed the same. It is true that in the final order of assessment, he gave no reasons. In the recent decision dated 30.7.2012 in the case of Gujarat Power Corporation Limited Vs. Assistant Commissioner of Income-tax in Special Civil Application No.29792 of 2007, a Division Bench of this Court had an occasion to consider a question whether during the course of original assessment, the Assessing Officer had examined certain claims by raising queries and due

response from the assessee with respect to such a claim but at the time of framing the assessment did not reject the claim without recording reasons, could it be stated that the Assessing Officer had formed an opinion and that therefore, any attempt on his part to reopen such assessment without any new additional material would amount to amere change of opinion?. In this context, the Revenue's contention that in such a case the Assessing Officer cannot be said to be formed an opinion and that reopening would be permissible, was rejected. In the present case, it is not even the stand of the revenue that in the original assessment, the Assessing Officer had not formed any opinion with respect to this particular contested issue. On record, the revenue itself has produced a statement of fact prepared by the Assessing Officer, although after recording reasons for reopening. In such note prepared by the Assessing Officer himself, he had recorded that during the course of assessment proceedings for the year 1997-98 the Assessing Officer had called for details of retrenchment compensation and also asked the assessee-Company to justify why such expenses should not be disallowed. It was further recorded that after considering the submissions of the Company, the

Assessing Officer accepted the company's stand and did not disallow the expenditure incurred on Voluntary Retirement Scheme. It is foregone conclusion that in the original assessment, the Assessing Officer examined the claim of deduction put forth by the petitioner-Company and accepted the same on merits after considering the assessee's submissions.

12) It is this claim which the Assessing Officer desires to revisit, for which impugned notice for reassessment has been issued. The basis of such reopening is the circular issued by the C.B.D.T on 23rd January, 2001. Two questions therefore arise. Firstly, what exactly did the C.B.D.T provide in such circular. In other words, did the circular mandate that all voluntary expenditures for retirement schemes should be disallowed by way of capital expenditure and second what would be the effect of the Board's circular, even if such a meaning can be read into the said circular.

13) We may at this stage, record the exact contents of the Board's circular dated 23rd January, 2001, which read as under:

"It is noticed that a number of assessee have resorted to restructuring of human resources, financial engineering etc. Invariably, ex-gratia payments are made in order to encourage such schemes to further long term advantage to the assessee by way of profitability, competitiveness and also to further induction of technology. Particular mention may be made of the Voluntary Retirement Scheme (VRS) of the banking sector in this connection. The question arises whether the ex-gratia amount is allowable as revenue expenditure. In this connection, the primary test is to see whether any enduring benefit has resulted to assessee by making an expenditure. In the event, the expenditure is laid out for acquiring or bringing into existence an asset or advantage for the enduring benefit of the business, it is properly attributable to capital and is of the nature of capital expenditure. If any such asset or advantage for enduring benefit of the business is thus acquired or brought into existence, it would be immaterial whether the source of payment was the capital or the income of the concern or whether payment was made once and for all or was made at installments. While it is not ordinarily easy to evolve a full-proof test for ascertaining whether in a given case, expenditure is capital or revenue, the assessing officers normally decide the character of expenditure on fact and circumstances of each case. They consider the nature and the ordinary course of business and the objects for which the expenditure has been laid out. Towards this purpose, the test of enduring benefit is a useful tool in considering the ex-gratia amount, prima-facie, as a capital expenditure. In this view of the matter, the expenditure, as said above, is to be treated as capital expenditure."

- 14) If we peruse the circular minutely, it only refers to general principles when a expenditure can be

stated to be a revenue in nature and lays down general guidelines for the Assessing Officer to follow while examining the claims of the assesseees for deduction as revenue expenditure amount expended as ex-gratia payment for retrenchment of employees under Voluntary Retirement Scheme. In fact the circular itself highlights that it is not ordinarily easy to evolve the full-proof test for ascertaining whether in a given case expenditure is capital or revenue. The circular further highlights that for the purpose of taking such a decision, the test of enduring benefit is a useful tool in considering the ex-gratia amount which would, prima-facie, be a capital expenditure.

15) We do not find that the C.B.D.T circular lays any firm guidelines for considering the expenditure in question as either revenue or capital in nature. It only refers to the general principles and in fact emphasize that it would be difficult to evolve a full-proof test for judging whether a particular expenditure is revenue or capital in nature. The Board also referred to the enduring benefit test as one of the tools for considering the nature of expenditure since such test is neither exclusive nor the sole test

to be applied in all cases.

16) The board's circular thus, in our opinion, only lays down general guidelines for the purpose of guiding the Assessing Officers while taking up the question of the nature of expenditure incurred by the assesseees by way of ex-gratia payment towards retrenchment compensation under a voluntary retirement scheme. The Assessing Officer, in the present case therefore, could not have blindly relied on such circular to hold a belief that in the present case, income chargeable to tax had escaped assessment.

17) Even otherwise, in our opinion, the Assessing Officer could not have issued the impugned notice on the basis of C.B.D.T circular. Learned counsel Mr. Bhatt may be correct in pointing out that the C.B.D.T, through its circular, could have brought certain aspects to the notice of the Assessing Officer, insofar as assessment was concerned. it had to be the opinion of the Assessing Officer alone which would prevail. In that view of the matter, the circular of C.B.D.T may be a trigger, on the basis of which, the Assessing Officer may himself be satisfied that income

chargeable to tax in a given case had escaped assessment. Such a circular by itself, in our opinion, cannot be the tangible material required for Assessing Officer to hold a belief that income chargeable to tax had escaped assessment. The Apex Court in the case of Commissioner of ***Income-tax Vs. Kelvinator of India Ltd.***, (2010) 320 I.T.R 561 (SC) has held that even post amendment in section 147 of the Act with effect from 1.4.1989, the concept of change of opinion has not been given a go-by. Even after the amendment in section 147, the Assessing Officer must have some tangible material to hold a belief that income chargeable to tax had escaped assessment.

18) Such tangible material may be something that the Assessing Officer did not notice at the time of original assessment either because the material did not form a part of the record itself or was not brought to his notice. In any case, the present circular of the C.B.D.T would not satisfy such a test. As already noted, the circular only lays down general reference and expected the Assessing Officers to examine the claim of assesseees or deduction of expenditure incurred towards retrenchment compensation

under Voluntary Retirement Scheme on the basis of the principles of enduring benefit. We may recall that this is neither the sole test to be applied nor did the C.B.D.T provide so in the circular in question. Thus on the basis of some general observation and discussion on principles for treating an expenditure either revenue or capital in nature, the Assessing Officer cannot claim to have been in possession of tangible material to hold a belief that income chargeable to tax had escaped assessment.

19) Quite apart therefore, from the question whether the circular of the C.B.D.T was opposed to law laid down by different courts and quite apart from binding effect of such circular on the assessee, we are satisfied that in the present case, notice for reopening has been issued without jurisdiction. In the result, the petition is allowed. The impugned notice dated 15.3.2001 is hereby quashed. Rule is made absolute with no order as to costs.

(AKIL KURESHI, J.)

(HARSHA DEVANI, J.)

Vahid

