



* **REPORTABLE**
IN THE HIGH COURT OF DELHI AT NEW DELHI

+ **[ITA 1856 OF 2010]**

% **RESERVED ON: 05.4.2011**
PRONOUNCED ON:11.5.2011

COMMISSIONER OF INCOME- TAX . . . **APPELLANT**
Through : Mr. Sanjeev Sabharwal,
Sr. Standing Counsel

VERSUS

MANAK SHOES CO. PVT LTD. . . . **RESPONDENT**
Through: Mr. S. Krishnan, Advocate.

CORAM :-

HON'BLE MR. JUSTICE A.K. SIKRI
HON'BLE MR. JUSTICE M.L. MEHTA

1. Whether Reporters of Local newspapers may be allowed to see the Judgment?
2. To be referred to the Reporter or not?
3. Whether the Judgment should be reported in the Digest?

A.K. SIKRI, J.

1. For the assessment year 2002-03, the assessee filed its return declaring 'NIL' income. The same was processed and assessed under the provisions of Section 143 (3) of the Income-Tax Act (hereinafter referred to as 'the Act') vide orders dated 30th September, 2004. However, thereafter, notice under Section 147 of the Act dated 18th September, 2006, was issued seeking to



reopen the assessment stating that the Assessing Officer had 'Reasons to Believe' that the income had escaped assessment within the meaning of Explanation 2 C(i) and (iv) of Section 147 of the Act. In the notice dated 18th September, 2006 following reasons were given:-

"It has come to notice that there is no manufacturing activity. However, on plant building, dies and moulds, wages, job work, repair maintenance has been claimed even though there was no production during the year."

Thus, according to the Assessing Officer, though there was no manufacturing activity during the previous year, still the assessee had claimed depreciation on plant, machinery, factory, dies and moulds etc. The assessee had also claimed expenses on power and fuel charges, job charges and raw material, even though there was no production during the year. The assessee filed objection against the reopening which was repelled by the AO vide orders dated 7th November, 2007. Thereafter, the AO passed assessment orders dated 12th November, 2007 as per which expenses of ₹ 67,14,144/- and depreciation of ₹ 32,15,385/- was disallowed.



2. The assessee preferred appeal thereagainst before the CIT (A). In this appeal, the assessee challenged the validity of notice dated 18th September, 2006 and initiation of reassessment proceedings on the ground that the assessee had no manufacturing activity in this year and this fact was duly brought to the notice of the AO at the time of original assessment proceedings. It was submitted that the assessee is engaged in the business of manufacturing shoes. Its promoters are overseas and the unit was set up to manufacture shoes for overseas market. During the year under consideration, the assessee company incurred huge losses in its manufacturing operations as it received no orders from its overseas buyers who were facing competition from Chinese made shoes. However, the assessee kept all its manufacturing facility intact at the behest of buyers and for maintaining the same, expenditure was incurred. The said expenditure was claimed from the promoters. The Assessing Officer allowed the entire expenditure in the original assessment. The assessee also got a reimbursement of ₹ 1.34 crores from its buyers as compensation for maintaining manufacturing facility. The same was taxed in entirety yet the Assessing Officer disallowed the expenditure so claimed in its return of income. These aspects were examined at the time of original assessment



and no new fact has come to light on the basis of which, reopening can be done.

3. The CIT (A) accepted the aforesaid contention of the assessee. In the order passed by him, it is mentioned that he had perused the return of income of the assessee company filed with the Department which was accompanied by P & L Account and Balance sheet and various schedules annexed thereto. Schedule 17 related to 'Significant Accounting Policy' wherein data on consumption of raw material, payment to auditors, production date on sport/casual shoes/sleepers and sales had been provided. Though there was no production during the year under consideration but still the assessee has shown sales amount to ₹ 4,70,570/- and job work income amounting to Rs 20,400/-. No new purchases have been made but the opening stock is shown at ₹ 30,01,843.87 and closing stock at ₹ 9,04,364.00 and all these figures are clearly discernible from the data available on the return of income. When these facts were available on record and the Assessing Officer had passed the original assessment order after scrutiny, then he was of the considered opinion that reopening had been resorted to by the officer on account of change of opinion. Since notice for reopening of the assessment was



quashed, the CIT (A) did not go into the merits of the expenses and depreciation disallowed by the AO.

14. The Revenue, obviously, felt aggrieved by this order and, therefore, approached the higher authority namely the ITAT by way of second appeal. However, it has not succeeded in the said attempt as its appeal had been dismissed by the Tribunal vide impugned decision dated 5th February, 2010 affirming the view of the CIT (A) that resort to Section 147/148 was unwarranted as it constituted a change of opinion since the material acted upon had been made available alongwith the return of income.

5. Still dissatisfied, present appeal is preferred by the Revenue under Section 260A of the Act in which following questions of law are proposed.

“1. Whether learned ITAT erred in holding that assumption of jurisdiction by the Assessing Officer under Section 147/148 was non-est and invalid.

2. Whether the notice under Section 148 issued by Assessing Officer for reopening the assessment is invalid and bad in law?”

6. Mr. Sabharwal, learned counsel appearing for the Revenue submitted that the notice under Section 148 of the Act was issued, when it came to light that there was no manufacturing activity by the assessee in the relevant previous year and in the absence of



any such manufacturing activity, the assessee was not entitled to depreciation. Likewise, in the absence of any such production, the assessee could not claim the expenses on power and fuel charges, job charges and raw material etc. According to him this case was squarely covered by Explanation 2 (c) (i) and (iv) of Section 147 of the Act which reads as under:-

“Explanation 2 : For the purposes of this section, the following shall also be deemed to be cases where income chargeable to tax has escaped assessment, namely :-

(a)

(b)

(c) Where an assessment has been made, but –

(i) Income chargeable to tax has been underassessed; or

(ii)...

(iii)...

(iv) Excessive loss or depreciation allowance or any other allowance under this Act has been computed.”

7. His submission was that while considering as to whether notice under Section 148 of the Act was validly issued or not, what was to be seen was that the matter was to be examined from the angle as to whether the reasons for reopening the assessment were justified or not. His submission was that in the present case, the Assessing Officer while framing the original assessment did not notice that there was no manufacturing



activity and no production by the assessee. He did not examine the issue as to whether there was any passive user of the machinery and the assessee was entitled to the depreciation or not. Thus, the reopening of the assessment was valid, and the ground on which assessment was opened was all together different matter. The assessee could still justify the machinery kept ready for use and, therefore, the assessee was entitled to claim depreciation and likewise, entitled to claim other expenditures. He also argued that merely because documents were submitted alongwith the return in the form of balance sheet etc. would not be a reason to presume that all these were looked into by the AO and the AO had applied his mind to the issue that the assessee was entitled to depreciation as there was a passive user of the machinery in question. He referred to and relied upon the judgment of this Court in **Rakesh Agarwal Vs. Assistant Commissioner of Income-Tax**, 221 ITR 492 wherein it was held as under:-

“It is true that in *Calcutta Discount Ltd. v. ITO* [1961]41ITR191(SC), the locus classicus on the subject, the Supreme Court did hold that the obligation of the assessed is to disclose only primary facts and not inferential facts. Primary facts are those which are material in that if taken into account, they would have an adverse effect on the assessed for assessment on greater income than what has been actually assessed. What facts are



material and necessary for assessment differ from case to case. Would mere filing of these documents amount to disclosure of primary facts is the question ? Indeed, the answer is given in the dissenting portion of the judgment by Hidayatullah J. (as his Lordship then was) in Calcutta Discount Co.'s case [1961]41ITR191(SC) saying that if some material for the assessment lay embedded in the evidence which the revenue could have uncovered but did not, then, it is the duty of the assessed to bring it to notice of the assessing authority because the assessed knows all the material and relevant facts-the assessing authority might not. These observations have been applied and reiterated in subsequent decisions of the Supreme Court and still hold the field.

To meet the contention of the assessed that once the afore noted documents had been produced before the Assessing Officer, there was no further obligation cast on him to disclose further facts, which on due diligence, the Assessing Officer might have discovered, Mr. Rajendra, learned counsel for the Revenue, has invited our attention to Explanation 2 (as it stood at the relevant time) to section 147, which runs as follows :

"Explanation 2. - 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 disclosure within the meaning of this section."

The language of Explanation 2 is self-explanatory and gives a quietus to the contention that where books of account or other evidence is produced before the Assessing Officer, there is no duty on the assessee to disclose further facts, which with



due diligence could be discovered by the Assessing Officer. The Explanation it itself makes it clear that mere production of evidence before the assessing authority would not per se be enough and there may be an omission or failure to make a full and true disclosure if some material for the assessment lay embedded in the evidence which the Revenue could have uncovered but did not (to repeat the words of Hidayatullah J., in Calcutta Discount Co.'s case [1962] 41 ITR 191). In Indo-Aden Salt Manufacturing and Trading Co. P. Ltd. v. [1986]159ITR624(SC) , the Supreme Court has further clarified, holding that the fact that the Assessing Officer could have found out the correct position by further probing the matter does not exonerate the assessed from the duty to make a full and true disclosure of the material facts. The court observed that Explanation 2 to section 147 makes the position abundantly clear.

At this stage we may notice the significance of the words "not necessarily" as appearing in Explanation 2. In our view, these words only indicate that whether there is a disclosure or not within the meaning of section 147(a) of the Act would depend on the facts and circumstances of each case. To put it differently it would be the nature of documents and the circumstances in which these are produced before the Assessing Officer that will determine the question. For instance, if material evidence is not writ large on the document but is embedded in come voluminous records/books of account requiring a careful scrutiny and delving deep into it to notice the necessary material, it is quite possible that having regard to the nature of the documents, material evidence cannot be discovered form such records despite due diligence and the case would attract application of Explanation 2 to hold that mere production of the books of account



or the documents, etc., without pointing out the relevant entries therein, does not amount to disclosure within the meaning of section [147\(a\)](#) of the Act.”

8. We are unable to persuade ourselves with the aforesaid submission of learned counsel for the Revenue. Reading of the original assessment order dated 30th September, 2004 brings out following aspects:-

- (i) This was an order passed under Section 143 (3) of the Act
- (ii) The assessment order specifically notices that the return accompanied by statutory audit report in Form 3CD.
- (iii) The case was taken up for scrutiny. First notice under Section 143 (2) was issued on 13.10.2003 and duly served upon the assessee. Thereafter, notice under Section 143(2)/142(1) of the Act alongwith questionnaire dated 1.6.2004 was issued for 24.6.2004. The representative of the assessee attended the proceedings pursuant to the said notice and supplied the details from time to time.
- (iv) The AO examined the details in respect of various items. He specifically recorded that “as in the



past the assessee continues to carry on the business of casual sports shoes”

- (v) Various items were scrutinized on merits and the issue on deprecation was also specifically commented upon on certain aspects inasmuch as certain expenses were disallowed holding that the assessee was not entitled to depreciation thereupon. This original assessment order unequivocally manifests that the AO specifically went into the issue as to whether there was a manufacturing activity or not.

9. In this background, we have to examine the assertion of the assessee that the assessee had subsequently informed the AO that it had incurred huge loss in its manufacturing operation as it received no orders from its overseas buyers who were facing competition from Chinese makers of shoes. It was also explained that the assessee had got all its manufacturing facility intact at the behest of the buyers and no expenditure for manufacturing the same was incurred. Most significant aspect is that the assessee had got a reimbursement of ₹ 1.34 crores from its buyers as compensation for maintaining the manufacturing facility which amount was offered for tax and was taxed in entirety even



though the AO disallowed the expenditure so claimed in its return of income. There is no reason, in the aforesaid circumstances, to disbelieve that the AO had not noticed that there was no manufacturing activity for want of orders, at the same time he allowed the depreciation keeping in view the aforesaid factors.

9. Again it is in this backdrop, we have to keep in mind that in support of its claim, the assessee had filed the profit and loss account and balance sheet of various schedules annexed thereto. Schedule 17 relates to "Significant Account Policy" wherein date of consumption of raw material, payment to auditors, production date on sport/casual shoes/sleepers and sales had been provided. The assessee had shown sales amounting to ₹ 4,70,570/- and job work income amounting to ₹ 20,400/-. It was on the basis of these facts which were available on record and when the original order passed by the AO reveals that there was an application of mind on the issue, there is no reason to presume that the AO would not have noticed the said material produced before him. On the aforesaid material and facts, the Tribunal has rightly concluded that it was a case of mere change of opinion and in the process observed as under:-

"It is not in dispute that originally, an assessment was completed by the Assessing Officer u/s 143 (3) of the Act. During the



course of the assessment proceedings, certain queries were raised by the Assessing Officer, which were duly replied to by the assessee and, thereafter, the Assessing Officer completed the assessment u/s 143(3) of the Act. The Assessing Officer, thereafter, issued a notice u/s 148 on 18.09.2006 by entertaining a belief that though there was no manufacturing activity during the previous year, the assessee had even claimed depreciation on plant and machinery etc. and has also claimed expenses on power and fuel, wages and job charges and raw material. The Assessing Officer had entertained a belief that income had escaped assessment by invoking the Explanation 2 (c) (i) and (iv) of Section 147 of the Act. From the reasons so recorded by the Assessing Officer, it is clear that no new facts or material came to the light after the assessment was originally completed u/s 143 (3) of the Act. On the basis of the same material or details available with the Assessing Officer at the time of completing the assessment u/s 143(3) of the Act, the Assessing Officer has entertained a believe that income chargeable to tax has been under assessed or excessive loss or depreciation allowance or any other allowances in this Act has been computed. It is also not the case of the Assessing Officer that any new material or fact came to his notice to entertain a belief that income had escaped assessment within the meaning of Section 147 of the Act”

10. Having regard to the aforesaid facts on record, judgment of **Rakesh Agarwal** (supra) relied upon by the learned counsel for the Revenue would have no application to the present case. In **Rakesh Agarwal** (supra), the Court held that mere production of evidence before the assessing authority would not per se be



enough as there may be an omission or failure to make a full and true disclosure if some material for the assessment lay embedded in the evidence which the Revenue could have uncovered but did not. The Court emphasized that whether there is a disclosure or not within the ambit of Section 147 (a) of the Act would depend upon the facts and circumstances of each case. One will have to consider the nature of documents and the circumstances in which those documents are produced before the AO. The Court gave an example of a case where material evidence was large number of the documents but was embedded in some voluminous records/books of accounts requiring a careful scrutiny and delving deep into it to notice the necessary material. In such a case, mere production may not amount to disclosure within the meaning of aforesaid provision. In the present case, however, as noted above, the AO had specifically taken note of the documents on record. The assessment order itself mentions that the return was accompanied by statutory audit report in Form 3 CD. The AO also applied his mind while examining the details in respect of various items as indicated above. Therefore, it cannot be said that it was a case of non disclosure.

11. For these reasons, we answer the question in affirmative in favour of the assessee and against the Revenue and consequently,



we do not find any merit in the appeal which is accordingly dismissed.

**(A.K. SIKRI)
JUDGE**

**(M.L. MEHTA)
JUDGE**

**MAY 11,2011
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