Modi Spinning and Weaving Mills Co. Ltd

Vs

Income-Tax Officer, Special Investigation Circle (B), Meerut

Civil Appeals Nos. 890-892 of 1968

(J.C. Shah, V. Ramaswami - I JJ)

10.02.1969

JUDGMENT

SHAH, J. -

1. Messrs Modi Spinning & Weaving Mills Co. Ltd. - hereinafter called 'the Company' - was incorporated in 1946. From time to time the Company purchased and installed machinery of the value of Rs. 75 lakhs for its factory. In proceedings for assessment of income-tax, the Company was allowed, in computing its income from business for the assessment years 1950-51, 1951-52 and 1952-53 initial depreciation aggregating to Rs. 15,91,511/- in respect of new machinery installed in the relevant previous years. The Company was also allowed normal depreciation at the appropriate rates. In the assessment year 1956-57 the aggregate of all depreciation allowances including initial depreciation exceeded the original cost of the machinery, but the Income-tax Officer on the written down value of the machinery computed at Rs. 16,48,053/- allowed Rs. 2,59,236/- as normal depreciation. In so computing the normal depreciation the Income-tax Officer apparently lost sight of clause (c) of the proviso to Section 10(2)(vi) of the Income-tax Act, 1922. Depreciation allowance was also allowed in the assessment years 1957-58 and 1958-59 as a percentage on the appropriate written down value in those years. The Income-tax Officer on November 20, 1964, issued notices of re-assessment for the three years under Section 148 of the Indian Income-tax Act, 1961, which had replaced the Act of 1922. The Company filed under protest fresh returns and objected to the issue of the notices of re-assessment.

2. The Company also moved petitions in the High Court of Allahabad for writs quashing the three notices, contending, inter alia, that the notices issued more than four years after the expiry of the years of assessment were barred. At the hearing of the petitions counsel for the Company conceded that under proviso (c) to Section 10(2)(vi) of the Indian Income-tax Act, 1922, in the form in which it stood in the assessment year 1956-57 and thereafter, excessive depreciation was in fact allowed to the Company. It was also common ground that by virtue of clause (c) to Explanation 1 of Section 147 of the Income-tax Act, 1961, income having been made the subject-matter of excessive relief under the Indian Income-tax Act, 1922, the income chargeable to tax has escaped assessment. But it was urged that the income had not escaped assessment "by reason of the omission or failure on the part of the assessee to disclose fully and truly all material facts necessary for assessment of that year", for - (1) the Indian Income-tax Act, 1922, and the forms of returns prescribed under the rules did not require the assessee to disclose that initial depreciation had been allowed in the earlier years; and (2) that in any event the Income-tax Officer knew that initial depreciation had been allowed to the Company in the years 1950-51, 1951-52 and 1952-53.

3. R. S. PATHAK, J., who heard the petitions held that the Company committed no error in failing

to take into account the initial depreciation while entering the written down value in column (2) of Part V of the return. But the learned Judge held that it was incumbent upon the Company to inform the Income-tax Officer of all material facts necessary to make out its claim to depreciation and it was not open to the Company to set out only those facts which exaggerated its claim : the Company was bound to disclose all material facts which went to show what the true amount of the allowance were to which it was entitled. The learned Judge accordingly rejected the petitions. The order passed by Pathak, J., was confirmed in appeal under the Letters Patent.

4. By clause (vi) of sub-section (2) of Section 10 of the Income-tax Act, 1922, as amended by Act 8 of 1946, in computing the profits or gains of business, profession or vocation carried on by him, an assessee was entitled to allowances not only of normal depreciation but also initial depreciation at the rates set out in clauses (a), (b) & (c) in respect of buildings which had been newly erected, or the machinery or plant being new had been installed after the 31st day of March, 1945. It was, however, expressly enacted that the initial depreciation was not deductible in determining the written down value for the purpose of clause (vi). Allowance for initial depreciation was therefore not to be taken into account in determining the written down value for determining the normal depreciation. But on that account proviso (c) to Section 10(2)(vi) was not modified.

5. The written down value of the machinery of the Company in the year 1956-57 was Rs. 16,48,053/-, but for the application of clause (c) of the proviso to Section 10(2)(vi) the initial depreciation allowed in the years 1950-51, 1951-52 and 1952-53 had to be taken into account. The Income-tax Officer inadvertently failed to take into account the initial depreciation, and the Company was allowed normal depreciation in the year 1956-57 in excess of the amount permissible under proviso (c) to Section 10(2)(vi). The Income-tax Officer later sought to rectify the error and to bring to tax the income which had escaped tax.

6. Before R. S. Pathak, J., it was contended that the definition of "written down value" in Section 10(5)(b) applies whenever the expression is used in Section 10(2) and on that account the Company in setting out the written down value in column (2) of Part V of the return was obliged to take into account all the depreciation actually allowed to it including the initial depreciation and as the Company computed the written down value only by deducting the normal depreciation and not the initial depreciation it failed to disclose fully and truly all material facts necessary for the purpose of assessment. This argument was not accepted by the learned Judge. But he was still of the opinion that the Act imposed upon the Company a duty to disclose all material facts which went to show the true amount of the allowances to which it was entitled, and the Company by failing to disclose that initial depreciation had been allowed in three earlier years, the Company had failed to disclose fully and truly all material facts necessary for assessment, and on that account Section 147(1)(a) was attracted and the notice was properly issued.

7. In appeal, the High Court observed that the "only question for consideration" was whether the Income-tax Officer was justified in issuing a notice under Section 148 of the Income-tax Act, 1961. After stating that there was apparently "a mistake and error on the side of the Company as well as the Income-tax Officer", the Court observed that the Income-tax Officer could reasonably come to the conclusion that it was due to the omission and failure on the part of the assessee in disclosing fully and truly all material facts necessary for the assessment that the error was committed by the Income-tax Officer as a result of which some income had escaped assessment. The High Court then observed :

> "It is difficult to hold that the Income-tax Officer while issuing the notices under

> Section 148 of the new Act could not reasonably hold the view that prima facie the assessee was responsible for the escape in the assessment."

and held that the notices were not liable to be quashed.

8. Section 34(1)(a) of the Income-tax Act, 1922, provided :

> "(1) If -
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> (a) the Income-tax Officer has reason to believe that by reason of the omission or failure on the part of an assessee to make a return of his income under Section 22 for any year or to disclose fully and truly all material facts necessary for his assessment for that year, income, profits or gains chargeable to income-tax have escaped assessment for that year, or have been under-assessed, or assessed at too low a rate, or have been made the subject of excessive relief under the Act, or excessive loss or depreciation allowance has been computed, or
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> he may X X X proceed to assess or re-assess such income, profits or gains or re-compute the loss or depreciation allowance; and the provisions of this Act shall, so far as may be, apply accordingly as if the notice were a notice issued under that sub-section."

Section 34 confers jurisdiction upon the Income-tax Officer to issue a notice in respect of the assessment beyond the period of four years, but within a period of eight years, from the end of the relevant year, if two conditions exist - (1) that the Income-tax Officer has reason to believe that income, profits or gains chargeable to income-tax had been under-assessed; and (2) that he has also 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 Section 22, or (ii) omission or failure on the part of an assessee to disclose fully and truly all material facts necessary for his assessment for that year. These conditions are cumulative and precedent to the exercise of jurisdiction to issue a notice of re-assessment. Calcutta Discount Co. Ltd. v. Income-tax Officer, Companies District I Calcutta and Another. (41 ITR 191).

9. In deciding the appeal, the High Court held that the Income-tax Officer did in fact decide that the income had escaped assessment, but the High Court did not consider whether the income escaped assessment by reason of omission or failure on the part of the Company to disclose fully and truly all material facts necessary for assessment.

10. The judgment of the High Court is set aside and the case is remanded for determination of the question whether by reason of the omission or failure on the part of the Company to disclose fully and truly all material facts necessary for assessment of the Company for the three years in question, any income, profits or gains chargeable to income-tax have escaped assessment or the Company has been given excessive depreciation allowance in computing its income.

Costs of these appeals will be costs in the High Court. One hearing fee.

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