

Commissioner of Income-Tax, Bangalore

Vs

Shree Manjunathesware Packing Products & Camphor Works

(G. T. Nanavati, M. Jagannadha Rao JJ)

02.12.1997

JUDGMENT

NANAVATI, J.

1. Leave granted.

2. Heard learned counsel on both the sides.

3. This appeal arises out of the judgment and order passed by the High Court of Karnataka on 6th June, 1995 in I.T.R.C.No.26/93. The question that was referred to the High Court was:

"Whether, on the facts and in the circumstances of the case, the Appellate Tribunal is right in law in holding that the word 'record' used in Sec.263 (1) of the Act would not mean the record as it stands at the time of examination by the Commissioner, but it means the record as it stands at the time the order in question was passed by the ITO?"

4. The respondent-firm, during the previous year relevant to the assessment year 1977-78, had constructed a cinema theatre and in the return filed by it had shown the cost of construction at Rs.20,28,498/- (Rs.23,78,242 less Rs.3,49,644 being electric portion). The Income-Tax Officer on 2nd February, 1980 wrote to the Departmental Valuation Officer to ascertain and report correct cost of construction of the theatre. The Valuation Officer expressed his inability to give his valuation report by 31st March, 1980 by which date the assessment was to be completed. The Income-Tax Officer, therefore, without waiting for his report, passed an order of assessment accepting the valuation mentioned by the assessee in its return. The Valuation Officer submitted his report on 16th December, 1980. He determined the cost of construction at assessee. Therefore, the Commissioner of Income-Tax issued a notice under Section 263 (1) of the Income-Tax Act to the assessee on the ground that investment not accounted for by the assessee firm should have been brought to tax and the Income-Tax Officer having not done so, his order was erroneous and prejudicial to the interest of the Revenue. Before the Commissioner, it was contended by the assessee that as the Valuation report was not available to the Income-Tax Officer at the time of passing the assessment order and did not form part of the record of the proceeding, it could not be a valid basis for initiating an action under Section 263 of the Act and, therefore, the proceeding deserved to be dropped. The decision of the Calcutta High Court in Ganga Properties Vs.I.T.O., [(1979) 118 ITR 447] was relied upon in support of that contention. The Commissioner rejected it on the ground that the term 'record' would include all records available at the time of examination by him, set aside the assessment made by the Income-Tax Officer and directed him to pass a fresh assessment order in light of the observations made by him.

5.The assessee preferred an appeal to the Income Tax Appellate Tribunal against that order.The Tribunal upheld the contention of the assessee relying upon the judgment of the Calcutta High Court in Ganga Properties case (supra), allowed the appeal and set aside the order passed by the Commissioner.

6.At the instance of the Revenue, the question stated above was referred to the High Court of Karnataka for its opinion.The High Court after referring to the decisions of the Calcutta High Court in Ganga Properties case and C.I.T. Vs.S.M.Oil Extraction Pvt.Ltd.[(1991) 190 ITR 404], held that though the record contemplated by Section 263 (1) does not mean only the order of assessment but it comprises all proceedings on which the assessment is based, yet if there was some record which was not available on the date of compilation of assessment that record would not form part of the order of the assessment authorities.It, therefore, answered the question in affirmative, i.e., in favour of the assessee and against the Revenue.The Revenue has, therefore, filed this appeal.

7.Mr.Shukla, learned counsel for the Revenue, submitted that in view of the amendments made in Section 263 (1) by the Finance Act of 1988 and the Finance Act of 1989, the term 'record' would mean all records relating to that proceeding available at the time of examination by the Commissioner.He further submitted that even though the Valuation Report submitted by the Departmental Valuation Officer was not available to the Income-Tax Officer when he had passed the assessment order, as it was called for by him before passing of the assessment order, it became a part of the record and, therefore, it was open to the Commissioner to consider the same while exercising his revisional power under that section.Strongly opposing these submissions, Ms.Indu Malhotra, learned counsel appearing for the assessee, submitted that as the Commissioner had passed the order on 3rd March, 1982, the amendments made in Section 263 (1), in 1988 and 1989, though with retrospective effect cannot have the effect of validating the order of the Commissioner which was illegal when passed.She submitted that when the order was passed by the Commissioner the correct position of law was that only that record which was available to the Income-Tax Officer could be considered by the Commissioner for the purposes of exercising his power under Section 263 (1).She submitted that the legislature by adding the explanation and widening the definition of the term 'record' has now enabled the Commissioner to take into consideration all records relating to the proceeding.In her submission, the 1989 amendment had only limited retrospective effect.If an order passed by the Commissioner under Section 263, after 1st June, 1988 the material, which was not available to the Income-tax Officer, when he had passed the assessment order, then its validity had to be determined on the basis that not only all the record of that proceeding but the record relating to it was also available to the Commissioner.But an order passed before 1st June, 1988, if it was illegal for the reason that it had taken into consideration other material also, then the amendment of 1989 did not have the effect of making it legal.

8.Earlier Section 263 (1) did not contain any explanation. It enables the Commissioner to call for and examine the record of any proceeding under the Act and pass such order thereon as the circumstances of the case justify, including an order enhancing or modifying the assessment or cancelling the passed by the assessing officer is erroneous insofar as it is prejudicial to the interests of the Revenue. By the Taxation Laws (Amendment) Act, 1984, an explanation was added to Section 263 (1) for removal of certain doubts but it is not necessary to refer to that explanation as it related to the meaning of the expression" order passed by the assessing officer" and, therefore, not relevant for the purpose of this case.By the Finance Act, 1988, the said explanation as substituted w.e.f.Legislature had to make that amendment is stated in the Memorandum explaining the provisions in the Finance Bill of 1988.We will refer to only that part which is relevant for us.It was observed by the Legislature that the provision as it stood then, had given rise to judicial controversy

in respect of the following:

"48. x x x x x x

(a) On the interpretation of the term 'record': It has been held in some cases that the word 'record' in section 263 (1) could not mean the record as it stood at the time of examination by the Commissioner but it meant the record as it stood at the time when the order was passed by the Assessing Officer. Such an interpretation is against the Legislative intent and defeats the very objective sought to be achieved by such provisions, since the purpose is to revise the order on the basis of the record as is available to the Commissioner at the time of examination. x x x x x To eliminate litigation and to clarify the legislative intent in respect of the provisions in the three Direct Tax Acts, it is proposed to clarify the legal position in this regard in the Explanation to the relevant sections. The proposed amendments are intended to make it clear that 'record' would include all records relating to any proceedings under the concerned direct tax laws available at the time of examination by the Commissioner."

The relevant part of the explanation after its substitution read as follows:

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

(a) .....

(b) "record" includes all records relating to any proceeding under this Act available at the time of examination by the Commissioner,

(c).....".

9. Thus, by this amendment, definition of the term "record" for the purpose of Section 263, was provided by the legislature. But a doubt regarding the meaning of the term 'record' still persisted and, therefore, a further amendment was made by the Legislature while enacting Finance Act of 1989. The Memorandum explaining the provisions in the Finance Bill, 1989 makes that clear. Paragraph 28 of the said Memorandum reads as under:

28. Under the existing provisions of section 263 of the Income-tax Act and corresponding provisions of the Wealth-tax Act and the Gift-tax Act, the Commissioner of Income-tax is empowered to call for and examine the record of any proceeding and if he considers that the orders passed by the Assessing Officer is erroneous in so far as it is prejudicial to the interests of Revenue, he may pass such order thereon as the circumstances of the case justify, including an order enhancing or modifying the assessment, or canceling the same or directing a fresh assessment. By the Finance Act, 1988, an Explanation was substituted with effect from 1st June, 1988, to the relevant sections of the Income-tax Act, Wealth-tax Act and Gift-tax Act to clarify that the term "record" would include all records relating to any proceeding available at the time of examination by the Commissioner. Further, it was matters except those which have been considered and decided in an appeal. The above Explanation was incorporated in the Finance Act, 1988, to clarify this legal position to have always been in existence. Some Appellate Authorities have, however, decided that the Explanation will apply only prospectively, i.e., only to

those orders which are passed by the Commissioner after 1.6.1988. Such an interpretation is against the legislative intent and it is, therefore, proposed to amend section 263 of the Income-tax Act, so as to clarify that the provisions of the Explanation shall be deemed to have always been in existence. Amendments on the above lines have been proposed in section 25 of the Wealth-tax Act and section 24 of the Gift-tax Act also."

10. After that amendment, the relevant part of the Explanation reads as under:

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

(a) .....

(b) "record" shall include and shall be deemed always to have included all records relating to any proceeding under this Act available at the time of examination by the Commissioner;"

11. After referring to the history of this provision, we will now refer to the decisions, which were relied upon by the learned counsel in support of the rival contentions with respect to the correct interpretation of the word "record". The Calcutta High Court in *Ganga Properties Vs. Income-tax Officer* [(1979) 118 ITR 447], after observing that provision of Section 263(1) of the Act has to be understood on its own language and in the context of the revisional jurisdiction of the Commissioner conferred by it and also the scheme of the Act, held as under :

"Whereas s. 263(1) of the Act uses the words "is erroneous" and not the words "has become subsequently erroneous". Under this section, the Commissioner may call for and examine "the record" of the "proceeding" in order to consider in his revisional jurisdiction as to whether the order in question by the ITO "is erroneous". Therefore, he is to call for the "record" of the "proceeding" which was before the ITO and examine it in order to consider whether on the basis of the material which were before the ITO and formed part of that record the order passed by the ITO is "erroneous" and prejudicial to the interests of the revenue. Therefore, the materials which were not in existence at the time the assessment was made but afterwards came into existence cannot form part of the record of the proceeding of " \_ the ITO at the time he passes the order and accordingly, it cannot be taken into consideration by the Commissioner for the purposes of invoking his jurisdiction under this section, for he is not an appellate authority under this section and exercise only revisional jurisdiction and hence he can only take into consideration the record as it stood before the ITO and the materials in such record for the purposes of ascertaining whether the order in question was erroneous and prejudicial to the interests of the revenue.

In other words, any material which comes into existence later on cannot form part of the record of the ITO for the purposes of invoking the Commissioner's power under s. 263(1) of the Act. And it is only after the proceeding is lawfully initiated by the Commissioner on the basis of the record of the ITO that the Commissioner can take into account any material which may come into existence later on in view of the expression "after making or causing to be made such enquiry as he deems necessary" used in the second limb of this section." The Calcutta High Court interpreted the

word "record" under Section 263(1) before it was amended by the Finance Acts of 1988 and 1989. Following that decision Kerala High Court in Commissioner of Income-Tax Vs. M.A. Unneerikutty [(1992) 194 ITR 546], also took the same view. In that case attention of the Kerala High Court was drawn to the amendments made by Finance Acts of 1988 and 1989. The High Court, however, did not consider the effect of the said amendments as it was of the view that there was no occasion for the Tribunal to consider the scope of the amended Section because it came into force only in 1988, much later than the order disposing of the revision and, therefore no such question arose out of the order off the Tribunal. It was submitted by the learned counsel for the respondent that Section 263(1) was thus interpreted by the Calcutta and Kerala High Courts before it was amended in 1988 and 1989 and, therefore, that was the correct legal position till 1st June, 1988. The learned counsel also drew our attention to the decision of Allahabad High Court in Commissioner of Wealth Tax Vs. Raj Narain Pratap Narain (HUF) [(1989) 177 ITR 34]. In that case, in the wealth-tax proceedings for the assessment years 1978-79 and 1979-80 the Assessing Officer had determined the fair market value of an immovable property at Rs.7,35,086/- as on the two valuation dates relevant for the years in dispute. After the completion of those assessments, the Commissioner of Wealth-tax, on coming to know that the property was sold by the assessee on August 18, 1983 for a consideration of Rs.36 lakhs, initiated proceeding under Section 25(2) of the Wealth-Tax Act and subsequently passed an order holding the impugned assessment orders erroneous and prejudicial to the interests of the revenue. On appeal by the assessee, the Income Tax Appellate Tribunal held that "the expression "record" in section 25(2) of the Act cannot mean the record as it stands at the time when the action under that section is taken but it means the record as it stands when the assessment order was passed by the assessing officer". In support of this view the Tribunal had relied upon the decision of the Calcutta High Court in Ganga Property's (supra). Against the order of the Tribunal the Commissioner of Wealth Tax had preferred two applications under Section 27(3) of the Wealth-Tax Act but they were rejected by the High Court. The view taken by the Allahabad High Court was that the question raised by the Department was academic because the Tribunal had not passed its order entirely on the meaning of the expression "record" and the other reasoning on which the decision of the Tribunal was based was a factual one and was equally fatal to the cause of revenue. This decision is, therefore, of not any help at all.

12. She further submitted that in a matter arising under the Wealth-tax Act Gujarat High Court had also taken the same view and the Department's special leave petitions Nos. 8511-13 of 1984 (Commissioner of Wealth-tax Vs. Rajshree S. Parekh) [(1991) 191 ITR Statute p.76] though were heard after the said two amendments, this Court dismissed them summarily and thus the view taken by the Gujarat High Court was upheld. In that case the Wealth-tax Officer had assessed the assessee's property as per the approved valuer's report. The Commissioner in suo motu revision directed valuation in accordance with the departmental valuer's report. The Tribunal allowed the assessee's appeal against the order passed by the Commissioner and also rejected the Department's reference application. The High Court also rejected the reference application made by the Department. Aggrieved by the view taken by the High Court the Department had filed the said special leave petitions in this Court. It is true that the said special leave petitions were dismissed summarily but that would not mean that this Court approved the view that was taken by the High Court. 13. In a later decision in Commissioner of Income-Tax Vs. S.M. Oil Extraction Pvt. Ltd. [(1991) 190 ITR 404], Calcutta High Court itself interpreted the word "record" differently. In that case the assessment was completed on February 1, 1983. The Income Tax Officer before he completed the assessment had referred the matter of plant and machinery and electrical installation to the Valuation Officer (P & M). His report was not received by the

Income Tax Officer when the assessment was completed. It was received by him after the assessment proceeding was completed. The Commissioner of Income-Tax took into consideration the said Valuation Report and found the assessment order erroneous. In that context the question which had arisen for consideration was whether the Commissioner in exercise of jurisdiction under Section 263(1) of the Act could have relied upon the valuation report which had come into the possession of the Income-Tax Officer subsequent to the completion of the assessment. The Calcutta High Court held that "the record contemplated in section 263(1) does not mean only the order of assessment but it comprises all proceedings on which the assessment is based. The Commissioner is entitled, for the purpose of exercising his revisional jurisdiction, to look into the whole evidence. The expression "record" as used in section 263 of the Act is comprehensive enough to include the whole record of evidence on which the original assessment order was passed. The valuation proceeding is a part of the assessment proceeding. But once the valuation report was received by the Income Tax Officer, although subsequent to the completion of the assessment, it forms part of the assessment year in question". It further held that "where any proceeding is initiated in the course of the assessment proceeding having a relevant and material bearing on the assessment to be made and the result of such proceeding was not available with the Income-Tax Officer before the completion of the assessment, but the result came subsequently, the revising authority is entitled to look into such material as it forms part of the assessment records of the particular assessment year" Calcutta High Court took this without referring to the definition of the word "record" contained in the explanation to Section 263(1) of the Act.

14. It, therefore, cannot be said, as contended by the learned counsel for the respondent, that the correct and settled legal position, with respect to the meaning of the word "record" till 1st June, 1988, was that it meant the record which was available to the Income Tax Officer at the time of passing of the assessment order. Further, we do not think that such a narrow interpretation of the word "record" was justified, in view of the object of the provision and the nature and scope of the power conferred upon the Commissioner. The revisional power conferred on the Commissioner under Section 263 is of wide amplitude. It enables the Commissioner to call for and examine the record of any proceeding under the Act. It empowers the Commissioner to mark or cause to be made such enquiry as he deems necessary in order to find out if any it is prejudicial to the interests of the revenue. After examining the record and after making or causing to be made an enquiry if he considers the order to be erroneous then he can pass the order thereon as the circumstances of the case justify. Obviously, as a result of the enquiry he may come in possession of new material and he would be entitled to take that new material into account. If the material, which was not available to the Income-Tax Officer when he made the assessment could thus be taken into consideration by the Commissioner after holding an enquiry, there is no reason why the material which had already come on record though subsequently to the making of the assessment cannot be taken into consideration by him. Moreover, in view of the clear words used in clause (b) of the explanation to Section 263(1), it has to be held that while calling for and examining the record of any proceeding under Section 263(1) it is and it was open to be Commissioner not only to consider the record of that proceeding but also the record relating to that proceeding available to him at the time of examination.

15. The view that we are taking receives support from the two decisions of this Court, though the point which is raised before us was not specifically raised in those two cases. In Tax Reference Case No.11 of 1983 (The Commissioner of Income-Tax, Gujarat-I Vs. Shri Arbuda Mills Ltd.) this Court after considering the effect of the amendment made in Section 263(1) of the Act by the Finance Act, 1989 whereby clause c of the explanation was also amended with retrospective

effect from 1st June, 1988, held that "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 those items had not been considered and decided in the appeal filed by the assessee". In that case the assessment was completed on 31.3.1978 and the Income Tax Officer while computing loss and income of the assessee had accepted the claim of the assessee in respect of those three items. Obviously, in the appeals filed by the assessee those items were not the subject-matter of the appeals as the decision in respect thereof was in its favour. In respect of those three items the Commissioner had exercised his power under Section 263 of the Income-Tax Act and, therefore, the question which had arisen for consideration was "whether on the facts and in the circumstances of the case, the order of assessment passed by the ITO u/s 143(3) read with section 144B on 31.7.1978 had merged with that of the Commissioner (Appeals) dated 15.12.1979 in respect of the three items in dispute so as to exclude the jurisdiction of the Commissioner of Income-Tax under sec. 263"? Thus the amendment made in clause c was held applicable to the orders passed before 1st June, 1988.

16. In *South India Steel Rolling Mills. Madras Vs. Commissioner of Income Tax, Madras* [1997 (9) SCC 728], the Commissioner in exercise of his power under Section 263 had withdrawn the development rebate granted for the years 1962-63, 1963-64, 1967-68 and 1968-69 on the ground that since the partnership stood dissolved on 3.3.1968 on the death of one of the two partners, before the expiry of eight years the assessee firm was not entitled to the benefit of the development rebate under Section 33(1)(a) of the Act. The said order passed by the Commissioner was challenged before the Tribunal but the assessee's appeal had failed. At its instance the following question was referred to the Madras High Court:

"Whether on the facts and circumstances of the case the revision of assessment under Section 263 by the Commissioner for withdrawing the development rebate granted for Assessment Years 1962-63, 1963-64, 1967-68 and 1968-69 is proper and justified."

The High Court also decided against the assessee. In the appeal filed by the assessee the order of Commissioner was challenged inter alia on the ground that the power under Section 263 could have been invoked on the basis of the record as it stood when the order was passed by the Income Tax Officer and that it was not open to the Commissioner to take into account dissolution of the assessee firm, which took place after passing of the assessment order because that circumstance was not disclosed by the record which was before the Income Tax Officer. Rejecting this contention this Court held "As regards his taking into consideration an event which had occurred subsequent to the passing of the order by the Income-Tax Officer, it may be stated that in Explanation (b) in Section 263 there is an express provision wherein it is prescribed that "record shall include and shall be deemed always to have included all records relating to any proceeding under this Act available at the time of examination by the Commissioner". The death of one of the two partners resulting in the dissolution of the assessee firm on account of such death took place prior to the passing of the order by the Commissioner and it could, therefore, be taken into consideration by him for the purpose of exercising his powers under Section 263 of the Act." In that case also the amendment was held applicable to an order passed before 1st June, 1988.

17. We, therefore, hold that it was open to the Commissioner to take into consideration all the records available at the time of examination by him and thus to consider the Valuation Report submitted by the Department valuation Cell subsequent to the passing of the assessment order and, so the order passed by him was legal. The High Court was wrong in taking a contrary view. We, therefore, allow this appeal, set aside the judgment and order passed by the High Court and answer the question referred to the High Court in the negative i.e. in favour of the Revenue and against the assessee. In view of the facts and circumstances of the case, there shall be no order as to costs.