SUPREME COURT OF INDIA

Trustees of H.E.H. The Nizam's Supplemental Family Trust

Vs.

Commissioner of Income Tax

(D.P.Wadhwa and S.S.M.Quadri JJ.)

16.02.2000

JUDGMENT

D.P. WADHWA, J.

The question that calls for consideration is:

Whether, on the facts and in the circumstances of the case, the assessment made by the Income-tax Officer for the Assessment Year 1962-63 under Section 143(3) read with Section 147 of the Income Tax Act, 1961 is valid in law? The case concerns the H.E.H. the Nizam's second Supplemental Family Trust. The trustees of the trust filed income tax return for the Assessment Year 1962-63 on behalf of the beneficiaries on April 2, 1964. Along with the return they filed an application under Section 237 of the Income Tax Act, 1961 (for short the 'Act') for refund of tax of Rs.20,050.52 deducted at source on interest on Government securities and dividends. Section 237 of the Act provides for refund and it is as under: - "237. If any person satisfies the Assessing Officer that the amount of tax paid by him or on his behalf or treated as paid by him or on his behalf for any assessment year exceeds the amount with which he is properly chargeable under this Act for that year, he shall be entitled to a refund of the excess." Under Rule 41 of the Income Tax Rules, 1962 (for short the 'Rules') a claim for refund is to be made in Form No.

30. This Rule is as under: - "41.(1) A claim for refund under Chapter XIX shall be made in Form No.30.

(2) The claim under sub-rule (1) shall be accompanied by a return in the form prescribed under section 139 unless the claimant has already made such a return to the Assessing Officer.

(3) Where any part of the total income of a person making a claim for refund of tax consists of dividends or any other income from which tax has been deducted under the provisions of sections 192 to 194, section 194A and section 195, the claim shall be accompanied by the certificates prescribed under section 203.

(4) The claim under sub-rule (1) may be presented by the claimant in person or through a duly authorised agent or may be sent by post." The claim for refund is to be accompanied by return of income in the form prescribed under Section 139 of the Act unless the claimant has already made such a return to the Income-tax Officer.

Since there was no response from the Income-tax Officer the trustees reminded him on June 17, 1964 for disposal of the refund application. The Income-tax Officer gave a reply on July 22, 1964

stating that the refund could not be granted to the trustees unless the references on the same question for the preceding assessment years filed by the trustees were disposed of by the High Court. A reminder was again sent by the trustees on September 23, 1966 to the Income-tax Officer for grant of refund but again no reply was given by the Income-tax Officer. Thereafter a notice under Section 148 of the Act was received by the trustees from the Income-tax Officer requiring them to file return for the Assessment Year 1962-63. Return was filed on July 3, 1970 declaring an income of Rs.6, 26,200/- as long term capital gain. It would appear that on the same day the return was accepted on the income returned by the trustees.

The trustees thereafter raised an objection by writing to the Income-tax Officer on July 3, 1970, after they had received the assessment order, that the return filed by them on April 2, 1964 along with refund application was still pending and, therefore, the proceedings initiated under Section 147 of the Act were invalid. They also claimed that the assessment made pursuant to the notice under Section 148 was equally invalid. To this the Income-tax Officer sent his reply on July 16, 1970 stating that the return filed on April 2, 1964 was disposed of on November 10, 1965 by a note recorded by the Income-tax Officer in his file. This note was recorded on November 10, 1965 in the file pertaining to Assessment Year 1963-64 and was to the following effect: - "In view of the Supreme Court judgment in the case of H.E.H. Nizam, the question of giving credit for tax deducted at source can be considered in the hands of the beneficiaries. Hence, no credit for the tax deducted at source is to be allowed here. The question of refunding the additional surcharge will have to be considered." Against the order of reassessment dated July 3, 1970 trustees filed an appeal before the Appellate Assistant Commissioner questioning the same. The Appellate Assistant Commissioner took the view that the Income-tax Officer had not passed the final orders on the return filed on April 2, 1964 along with application seeking refund. He, therefore, held that the reassessment made by the Income-tax Officer pursuant to the notice under Section 148 of the Act was invalid and cancelled the same. The Revenue then took the matter in appeal to the Income Tax Appellate Tribunal.

Following two questions were raised before the Tribunal: - "(1) Whether the return filed by the assessee on April 2, 1964, along with the refund application was one filed under section 139(1) of the Income-tax Act? (2) Even if it is assumed that the return filed by the assessee along with the refund application commences assessment proceedings, whether the proceedings should be treated to have been finalised by the Income-tax Officer at least by his note dated November 10, 1965, if not earlier by his letter dated September 26, 1964, addressed to the assessee, and as the proceedings for the refund were terminated by the Income-tax Officer by his note dated November 10, 1965, there is no bar for the reassessment proceedings for the same year and, hence, the reassessment proceedings in respect of the income of such year would be valid?" There was difference of opinion between the Accountant Member and the Judicial Member comprising the Tribunal and the matter was referred to the third member in the following manner: - "Whether, on the facts and in the circumstances of the case, the order of assessment made by the Income- tax Officer for the Assessment Year 1962-63 under Section 147 of the Income-tax Act, 1961, is valid in law." The Accountant Member was of the view that the return filed by the assessee along with its refund claim did not set in motion any assessment proceedings and consequentially there were no assessment proceedings which remained undisposed of by the Income-tax Officer at the time when he initiated proceedings under Section 147 of the Act.

Judicial Member was of the view that on consideration of the entirety of the facts and circumstances of the case the return filed by the assessee on April 2, 1964 was a valid return. On second question whether proceedings had been terminated by the noting of the Income-tax Officer in the order sheet the Accountant Member held that proceedings, if any, that commenced with the return, were

terminated by the Income-tax Officer by his note dated November 10, 1965. On the second question the Judicial Member held that on a plain reading of the endorsement made by the Income-tax Officer it was very clear that no disposal was given to the return filed and the said endorsement related to the opinion expressed by the Income-tax Officer about giving credit for tax deduction at source. Third member (Mr. D. Rangaswamy, Vice President) after examining the whole matter said as under: - "Since I have already expressed my agreement with the views expressed by the Judicial Member that the return accompanying an application for refund is a return under section 139 and all the procedures, formalities and machineries applicable to proceedings of a return under section 139 would apply and I have further agreed with his view that there has been no termination of the proceedings, I hold that both the Judicial Member and the Appellate Assistant Commissioner were right in holding that the assessment made by the Income-tax Officer, pursuant to notice under section 147 was invalid and has to be accordingly cancelled." Thereafter, in conformity with the views of the majority of the members the Tribunal dismissed the appeal of the revenue.

At the instance of the revenue under Section 256(1) of the Act the Tribunal referred the question of law arising from its order to the Andhra Pradesh High Court as set out in the beginning of this judgment for the opinion of the High Court. High Court was of the view that the order dated November 10, 1965 of the Income-tax Officer on the note-sheet (reproduced above) was an order of disposal of the tax return filed by the trustees. It held that the return filed by the trustees on April 2, 1964 along with refund application was one filed under Section 139 of the Act and was valid return and as the refund application was disposed of by order dated November 10, 1965 of the Income-tax Officer, there was no bar to the reassessment proceeding for the same year and the reassessment proceedings were, therefore, valid.

Now it is the assessee, which felt aggrieved and has come to this Court. It is not disputed that the return filed with the refund application under Section 237 of the Act is a valid return and the Income-tax Officer can initiate proceedings for assessment on the basis of the return so filed. The only question that falls for consideration for us is: if in the circumstances of the case it could be said that the note recorded by the Income-tax Officer in his file on November 10, 1965 is an order which concluded the assessment proceedings for the Assessment Year 1962-63 before he initiated proceedings under Section 147 of the Act. It is also not disputed that this note/order of November 10, 1965 terminating the assessment proceedings for the Assessment Year 1962-63 was never communicated to the trustees till July 16, 1970 and that too in a reply to the letter sent by the trustees.

According to the High Court the note, which is an order, did terminate the assessment proceedings. High Court was of the view that the first part of the order gave reasons and the second part of the order clearly spoke of the conclusion when read: "Hence no credit for tax deducted at source is to be allowed here".

` It is settled law that unless the return of income already filed is disposed of notice for reassessments under Section 148 cannot be issued, i.e., no reassessment proceedings can be initiated so long as assessment proceedings pending on the basis of the return already filed are not terminated. According to the Revenue it is immaterial whether the order is communicated or not and that the only bar to the reassessment proceedings is that proceedings on the return already filed should have been terminated. In support of this contention reference was made to certain decisions of the High Courts and some observations made by this Court in a case, which we note as under:- In M.Ct. Muthuraman vs. Commissioner of Income-Tax, Madras [(1963) 50 ITR 656] the assessment proceedings which had commenced with the returns filed by the assessee were lawfully terminated

when they were closed with the entry "N.A." (not assessed). The orders terminating the assessment proceedings were not communicated to the assessee. The Income Tax Officer issued notices under Section 34 of the Income Tax Act, 1922 (corresponding to Section 147 of the Income Tax Act, 1961). The Court held that the assessment proceedings were lawfully terminated and that "the orders terminating the assessment proceedings were not apparently communicated to the assessee did not affect the legality of those orders or their finality".

In V.S. Sivalingam Chettiar vs. Commissioner of Income Tax, Madras [(1966) 62 ITR 678] again a similar question arose before the Madras High Court. It was contended that the conclusion of the Madras High Court in M.Ct. Muthuraman's case that "the orders terminating the assessment proceedings were not apparently communicated to the assessee did not affect the legality of those orders or their finality" was without reasons. But the Court rejected this contention and held : "But we are satisfied, if we may say so with respect, that that is the correct view to take.

Wherever orders are made under the Act, which affect the assessee in some form or other, it has provided for service of notice and the remedy there against. Section 29 requires notice of demand to be served on an assessee; but the section makes it a condition that a notice of demand will be required to be served only when any tax, penalty or interest is due in consequence of any order passed under or in pursuance of the Act. Learned counsel for the revenue argues that it is visualised by the section that there should be an order made under the Act under which tax, penalty or interest is due before a notice of demand is served, and that this means that service of notice does not bear on the validity of an order. In other words, what he points out is that there should be first a valid order, and then only a notice of demand is required to be served, so that service of notice is not a condition to the validity of the order itself. Though prima facie the argument may appear to be tenable, the question may arise as to whether proceedings under section 34 could be initiated between the date of an order under the Act and service of notice of that order. But an examination of some of the other provisions of the Act like sections 24(3), 23(5) and (6), 27, proviso (2) to section 30(1) and the related provisions in section 30 lead us to the conclusion that where orders are passed under or in pursuance of the Act, which are prejudicial to an assessee, notice of the order is required to be served and, for the purposes of resorting to the remedy, limitation is to count from the date of service of notice of such order. In this case, from a purely fiscal point of view, it can hardly be said that the orders made by the Income-tax Officer on the returns by the assessee as an individual were in any way prejudicial to him. The orders did not fasten on the assessee any liability to tax. Nor did they contain any finding which could by any means be said to be against the assessee as an individual. All that was held by the Income-tax Officer was that the income, which the assessee claimed to be his as an individual, did not belong to him.

That means that he was not held liable to pay any tax. In that sense, as it seems to us, not prejudiced as he was by the order passed by the Income-tax Officer, failure to serve notice thereof did not deprive these orders of their validity. In our view, on a strict reading of the Act, it does not appear to contemplate service of notice in such cases. Nevertheless, we feel that it is desirable from many points of view that the revenue serves notice on assessees of such orders. It will not only tend to fairness to the assessee but also avoid deserving complaints that an order of which the assessee was not aware of forms the basis of proceedings under section 34." Relying on these two decisions of the Madras High Court in M.Ct. Muthuraman and V.S. Sivalingam Chettiar's cases Kerala High Court in Commissioner of Agricultural Income-Tax, Kerala vs. K.H. Parameswara Bhat [(1974) 97 ITR 190] took somewhat a similar view. Kerala Agricultural Income Tax Appellate Tribunal under the Agricultural Income Tax Act, 1950, however, had taken the view that since the order of "nil" assessment had not been communicated to the assessee, the notice under Section 35 was ab initio

void.

The ground for the decision was that as far as the assessee was concerned, the assessement proceedings originally commenced were still pending because the order of "nil" assessment had not been communicated to the assessee. High Court said that the view taken by the Tribunal was erroneous. It said : "The scheme of the Act indicates that the making of an assessment naturally by an order is different from the communication of the assessment order to the assessee. There is no specific provision in the Act enjoining that an assessment order must be communicated to the assessee. Nor is there any provision in the relevant Rules that assessment orders must be communicated. All that section 30 of the Act requires is that a notice of demand in the prescribed form specifying the sum payable shall be served on the assessee when a tax or penalty is due in consequence of an order passed under the Act. But it is of course not only desirable but necessary that an order of assessment should be communicated to the assessee. The Act itself envisages service of the assessment order.

Sub-section (3) of section 31 for instance provides that an appeal from the order of assessment shall be presented within a period of thirty days from the date of service of the order. Apart from this, the assessee is entitled to know the reasoning for imposing tax or penalty on him and he would be able to exercise his right of appeal, if any, only if the order is communicated to him. But the questgion is not whether it is either desirable or necessary that an order of assessment should be communicated, but whether the lack of communication of the order would make the order void or would have the result of keeping the assessment proceedings pending. We conceive that once an order had been passed by the officer, it is not open to him to modify or alter that order even if the order had not been communicated to the assessee, without adopting the procedure prescribed by section 35 or section 36." In Kalyankumar Ray vs. Commissioner of Income Tax [(1991) 191 ITR 634] this Court said that the "assessment" is one integrated process involving not only the assessment of the total income but also the determination of the tax.

It said that when the Income Tax Officer first draws up an order assessing the total income and indicating the adjustments to be made, directs the office to compute the tax payable on that basis and then approves of it, either immediately or some time later, no fault can be found with the process, though it is only when both the computation sheets are signed or initialled by the Income-tax Officer that the process described in section 143(3) will be complete. Section 143(3) mandates that the Income-tax Officer "shall, by an order in writing, make an assessment of the total income or loss of the assessee, and determine the sum payable by him on the basis of such assessment".

In Commissioner of Income-Tax, Madras vs. M.K.K.R.

Muthukaruppan Chettiar [(1970) 78 ITR 69] it was observed that it was manifest that notice under Section 34 of the Income-Tax Act, 1922 for reassessment could not be issued unless the returns which had already been filed were disposed of. In that case the Income- tax Officer by his order closed the assessment as "no assessment" and added that since there was no separate income, the pending proceedings would be closed as N.A. and for income-tax year 1953- 54 the file would be removed and clubbed with the family file F. 1005-A. This Court said that the order of the Income-tax Officer should be interpreted in the light of the circumstances in which that order was passed and so interpreted "it appears to us that the Income-tax Officer did not intend to conclude the proceedings before him".

An order under Section 237 of the Act is appealable as provided in clause (k) of sub-section (1) of

Section 246 of the Act. Section 249 prescribes limitation for filing appeal. Sub-section (1) of Section 249 is relevant and it is as under : "249. (1) Every appeal under this Chapter shall be in the prescribed form and shall be verified in the prescribed manner (2) The appeal shall be presented within thirty days of the following date, that is to say (a) where the appeal relates to any tax deducted under sub-section (1) of section 195, the date of payment of the tax, or (b) where the appeal relates to any assessment or penalty, the date of service of the notice of demand relating to the assessment or penalty : Provided that, where an application has been made under section 146 for reopening an assessment, the period from the date on which the application is made to the date on which the order passed on the application is served on the assessee shall be excluded, or (c) in any other case, the date on which intimation of the order sought to be appealed against is served." There is difference in clauses (b) and (c) of sub-section (2) of Section 249 of the Act. Return of income filed in the form prescribed along with an application for refund under Section 237 of the Act is a valid return.

There is no stopping the Income Tax Officer to complete the assessment on the basis of return so filed. It may be that the Income Tax Officer may limit the scope of examination of the return to satisfy himself regarding the correctness of the amount claimed as refund. For that purpose, he will examine if the tax paid by the assessee exceeds the amount of tax for which he is chargeable. If it is found that the Income was "nil", he will direct refund be granted to the assessee for any amount of tax paid. That will certainly be assessment. Filing of return in the form prescribed under Section 39 of the Act along with the application for refund is not an empty formality. It assumes importance if such return had not been filed earlier. We have reproduced the note/order dated November 10, 1965 on the file pertaining to assessment year 1963-64. In the file for assessment year 1963-63 there is another note which is as under: "Please see my note in 1963-64 file. Refund to be considered in the hands of the beneficiaries." The mere glance at this note would show that it could not be said that the Income Tax Officer gave finality to the refund since no refund is granted either in the hands of the trust or in the hands of the beneficiaries. It is an inconclusive note where the Income Tax Officer left the matter at the stage of consideration even with regard to refund in the hands of the beneficiaries. This note was also not communicated to the trustees. When we examine the note dated November 10, 1965 on the file of 1963-64 nothing flows from that as well. In any case if it is an order, it would be appealable under Section 249 of the Act. Since period of limitation starts from the date of intimation of such an order, it is imperative that such an order be communicated to the assessee. Had the Income-tax Officer passed any final order, it would have been communicated to the assessee within a reasonable period. In any case, what we find is that the note dated November 10, 1965 is merely an internal endorsement on the file without there being an indication if the refund application has been finally rejected. By merely recording that in his opinion, no credit for tax deducted at source is to be allowed the Income Tax Officer cannot be said to have closed the proceedings finally. Decisions referred to by the revenue are of no help in the present case. We are, thus, of the opinion that during the pendency of the return filed under Section 139 of the Act along with refund application under Section 237 of the Act action could not have been taken under Section 147/148 of the Act. Our answer to the question, therefore, is in the negative, i.e., against the Revenue. The appeal is accordingly allowed with costs.