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Validity of reassessment proceedings

The Hon'ble Supreme Court examined the validity of reassessment proceedings initiated on the taxpayer and held that they were invalid as pre-conditions required for initiation were not satisfied

Facts of the case:

- New Delhi Television Limited (taxpayer)¹ is an Indian company engaged in operating various television channels. The taxpayer has multiple foreign subsidiaries and the key issue pertained to the UK subsidiary, NDTV Network Plc., U.K. (NNPLC).
- In July 2007, NNPLC had issued step-up coupon bonds of US\$ 100 million (redeemable at a premium of 7.5% after a period of five years). The taxpayer agreed to furnish corporate guarantee for these bonds. However, these bonds were redeemed in advance, at a discounted price of US\$ 74.2 million.
- The taxpayer's case for the financial year (FY) 2007-08 corresponding to the assessment year (AY) 2008-09 was selected for audit. The Assessing Officer (AO) during the course of audit proceedings noted that NNPLC did not have financial net worth or any business and thus, NNPLC could not have issued bonds and raised money without the assurance from taxpayer. The AO did not doubt the validity of the transaction and imposed guarantee fee income of 4.69% on the taxpayer in his original order dated 3 August 2012.
- Subsequently, on 31 March 2015, the taxpayer was served with a notice under section 148 of the Income-tax Act, 1961 (ITA), stating that there was reason to believe that income relating to issuance of bonds by NNPLC for AY 2008-09, had escaped assessment and that the case should be reassessed. The AO gave the following reasons in support of the belief that income had escaped assessment:
 - In AY 2009-10, the Dispute Resolution Panel (DRP) had confirmed the addition proposed by the AO of INR 6.42 billion, for funds raised by the taxpayer through its overseas subsidiaries (including NNPLC). These transactions were held to be sham and bogus;
 - NNPLC was placed under liquidation on 28 March 2011;
 - Based on the DRP order for AY 2009-10 and complaints received from minority shareholders, the funds received by NNPLC during the FY 2007-08 corresponding to the AY 2008-09 were actually funds of the taxpayer;
 - The income had escaped assessment due to failure by the taxpayer to disclose fully and truly all facts material for audit.
- The taxpayer filed the following objections against the notice of the AO:
 - There was no failure to disclose fully and truly all facts material for audit;
 - The AO had changed his opinion;
 - The transaction of issue of step-up bonds was a legal and valid transaction;
 - The AO had no valid reason to believe that income had escaped assessment;

¹ 116 Taxmann.com 151(SC)

- The AO had treated the transaction to be genuine and levied guarantee fee income;
- Notice was issued beyond the time limit of four years and hence, invalid;
- Considering that all material facts were disclosed, the notice, being issued beyond a period of four years, was invalid.
- The AO rejected the objections of the taxpayer in his order dated 23 November 2015 holding that there was non-disclosure of material facts and the notice was issued within the time limit as NNPLC was a non-resident entity (through which income of taxpayer was derived) and time limit of 16 years² was applicable for issuance of reassessment notice.
- The taxpayer filed writ petition before the High Court against the AO's order. The High Court dismissed the taxpayer's writ.
- Aggrieved by the High Court's order, the taxpayer filed an appeal before the Hon'ble Supreme Court (SC).

Provisions which are relevant for the case under consideration, in brief:

- As per the provisions of the ITA, reassessment proceedings can be initiated (within a period of four years from the end of the relevant AY) if the AO has reason to believe that income has escaped assessment;
- In cases where income has escaped assessment due to failure on the part of the taxpayer to file an income-tax return or due to failure to fully and truly disclose all material facts necessary for audit and the AO has reason to believe, an extended time limit of six years (from the end of the relevant AY) is available for initiating reassessment;
- Further, in cases where there is reason to believe that income relating to asset located outside India has escaped assessment, an extended time limit of 16 years (from the end of the relevant AY) is available for initiating reassessment.

Decision of the Hon'ble SC:

- The Hon'ble Supreme Court noted that the following three issues had emerged for consideration:
 - i. Whether there was valid reason to believe that income had escaped assessment?
 - ii. Whether the taxpayer had disclosed fully and truly all material facts during the course of original audit?
 - iii. Whether, in facts of the case, the time limit of 16 years applied for issuance of the reassessment notice by the AO?
- At the outset, the SC held that a detailed audit proceeding did not take away the power of reassessment.
- Further, the Hon'ble SC mentioned that it was not going into the merits of the transactions.

Issue 1 – Whether there was valid reason to believe that income had escaped assessment?

- The SC noted the AO's reliance on the DRP order for AY 2009-10 (holding the transaction of overseas group companies as bogus and sham) passed after the completion of the original

² In cases of income relating to any asset (including financial interest in an entity) located outside India which has escaped assessment, time limit of 16 years is applicable for issuance of reassessment notice.

assessment proceedings for the AY 2008-09. Further, it took note of the complaints filed by the minority shareholders.

- The SC referred to various judicial precedents³ wherein it was held that facts received after completion of audit (including information received during the subsequent year audit) can be considered for reassessment.
- Further, the SC held that at the initial stage of issuance of notice, the AO only has to form a prima facie view.
- In view of the above, the SC held that in the case under consideration, material disclosed in audit proceedings for subsequent years was sufficient to hold that there were reasons to believe that income had escaped assessment.

Issue 2 – Whether the taxpayer had disclosed fully and truly all material facts during the course of original audit?

- The SC noted that the following material facts were provided by NNPLC to the officer conducting investigation vide letter dated 8 April 2011 and were also available with the AO:
 - i. Names of the bond holders along with their addresses; and
 - ii. Number of bonds issued along with consideration received.
- Further, the SC noted that the AO had information relating to issue and early redemption of bonds (at a discounted price) before completion of the original audit proceedings. The AO had also accepted issuance of the bonds and imposed guarantee fee income on the taxpayer in the original order.
- The SC also noted that the Revenue had not raised the issue relating to full and true disclosure of facts at the time of appeal before the High Court.
- The SC relied on an earlier case⁴, wherein it was held that the taxpayer is duty bound to fully and truly disclose material primary facts for the purposes of audit. Non-disclosure of other secondary facts is not necessary.
- The SC held that the taxpayer in the case under consideration, had disclosed all primary facts and was not required to give any further assistance to the AO for carrying out the audit. Thus, the benefit of the extended period of limitation of six years for issuance of a reassessment notice was not available.

Issue 3 – Whether, in facts of the case, the time limit of 16 years applies for issuance of the reassessment notice by the AO?

- The SC noted that the case of the AO was that as per the second proviso to section 147 read with section 149(1)(c) of the ITA, the limitation period was 16 years (and not four years) as the taxpayer derived income from NNPLC, a foreign entity.
- The SC noted that the notice initiating reassessment and the reasons for reassessment communicated by the AO to the taxpayer were silent and did not bear reference to the second proviso (relating to income earned from asset located outside India which has escaped assessment). The reasons for reassessment communicated by the AO were only reasons to believe and non-disclosure of material facts by the taxpayer.

³ Claggett Brachi Co. Ltd., London vs Commissioner of Income Tax, Andhra Pradesh 1989 Supp. (2) SCC 182; Phool Chand Bajrang Lal and Another vs Income Tax Officer and Another [1993] 4 SCC 77; Ess Kay Engineering Co.(P) Ltd. vs Commissioner of Income Tax, Amritsar [2001] 10 SCC 189

⁴ Calcutta Discount Co. Ltd. v. Income-tax Officer, Companies District I, Calcutta and Another AIR 1961 SC 372

- The SC held that the taxpayer must be provided in notice or reasons all the provisions of the ITA relied upon by the Revenue for reassessment. Not mentioning the provisions in the notice and reasons, do not conform to the principles of natural justice as the taxpayer did not get an opportunity to reply to the contentions of the AO for reassessment.
- In view of the above, the SC held that the notice issued to the taxpayer did not invoke the provisions of the second proviso which provides time limitation of 16 years for issuance of notice.
- The SC also held that the Revenue may issue a fresh notice if permissible under the law.

Observations:

- The ruling lays down the following key principles which may be relevant for taxpayers in connection with reassessment proceedings:
 - A detailed audit proceeding does not take away the power of reassessment;
 - Material disclosed during audit proceedings for subsequent years can form the basis for reassessment;
 - It is the duty of a taxpayer to disclose all primary material facts relevant for carrying out the audit proceedings;
 - The reassessment notice should clearly mention the provisions relied upon by the AO for initiating reassessment proceedings.



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