Published on *The National Law Review* https://natlawreview.com

Re-Assessment Notices Issued Under Erstwhile Provisions To Be Considered As Issued Under New Provisions: Supre Court

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Recently, The Supreme Court of India ("SC")[1] upheld the validity of the reassessment notices ("Notices")issued post April 1, 2021 under pre-amended section 148 of the Income Tax Act, 1961 ("ITA"). The SC adjudicated that the Notices shall be deemed to be issued under section 148A of the ITA and be treated as Show Cause Notice in terms of section 148A(b) of the ITA.

FACTS

Due to the onset of the Covid-19 pandemic, a Relaxation Act, 2020 was passed by the Central Government under which the Central Government issued notifications to extend the time limit for issuing Notices under various provisions of the (Indian) Income Tax Act, 1961. One such extension was for issuing notices for re-assessment under the pre-amended section 148 of the ITA. The limitation period under the relevant provision would expire on March 31, 2021 but with various notifications was extended to June 30, 2021, which means notices which could have been issued on or before March 31, 2021 could now be issued upto June 30, 2021. The explanation to these notifications stated that the provisions as existed prior to the amendments made by the Finance Act, 2021 shall apply to reassessment proceedings initiated thereafter as well.

On the basis of these notifications the Indian tax department post April 1, 2021 issued more than 90,000 Notices under pre-amended section 148 of the ITA to various assesses which became subject matter of more than 9000 Writ Petitions before various High Courts ("HCs").

HCs in numerous matters[2] ruled in the favour of assesses and observed that section 148A of the ITA which was introduced through the Finance Act 2021 is a remedial and benevolent provision in nature, and hence shall be applicable in each case wherein the notice under section 148 was issued after April 1, 2021. Since the Notices were issued by the Revenue under section 148 of the ITA without following the procedure laid down in section 148A, they are invalid in law and so should be quashed.

In response, the Revenue preferred an appeal before the SC.

SECTION 148 AND SECTION 148A OF THE ITA

Section 148 of the ITA allows the Assessing Offer ("AO") to issue Notice for initiating re-assessment

proceedings on tax payers. Section 148 of the ITA as it stood, prior to the amendment vide the Finance Act, 2021 was vaguely worded and allowed the AO to issue Notice whenever such AO had 'reason to believe' that income has escaped assessment. Moreover, the provision lacked to provide any safeguards or defences to the taxpayer. The crucial right to provide opportunity of hearing to the taxpayer and follow a proper procedure was also governed by the SC's judgement in the case of GKN Driveshafts (India) Ltd. v. Income Tax Officer[3]. Thus, the provision was ambiguous and led to unnecessary litigation.

To remove these difficulties and streamline and simplify tax administration, the Finance Act 2021 substituted section 147 to 151 of the ITA and also introduced section 148A. As per amended section 148, no Notice can be issued by the tax department ("Revenue") without following the procedure laid down in section 148A of the ITA. Further, the pre-requisite to issue Notice has been changed from 'reason to believe' to presence of 'information which suggests that income chargeable to tax has escaped assessment', which has also been properly defined. Additionally, section 148A also lays down various safeguards to protect the interest of the taxpayer being -

1. If required, prior to issuing Notice under section 148 of the ITA, the AOmay conduct enquiry with the approval of the specified authority in respect to the information which suggests that the income chargeable to tax has escaped assessment.

2. The AO will have to provide an opportunity of hearing the taxpayer with the prior approval of the specified authority.

3. The AO will have to mandatorily consider the reply filed by the taxpayer to the show cause notice issued him.

4. The AO will have to decide on the basis of material available and the reply furnished by the taxpayer that whether it is a fit case to issue a notice under section 148 of the ITA.

5. Lastly, the AO will have to pass the order within stipulated time period.

AMENDMENT TO LIMITATION PERIOD

The Finance Act, 2021 also reduced the limitation period for the issuance of Notices under Section 149 of the ITA. Previously, pre-amended section 149 of the ITA authorised the Revenue to issue Notice within 6 years of the filing of the annual return and in some exceptional cases upto 16 years. However, the amended provision restricts the limitation period for Revenue to issue Notices to only 3 years of filing of annual return. Further Notices can be issued beyond 3 years and upto 10 years only in specific cases where the Revenue has in his possession books of account or other documents or evidence which reveal that the income chargeable to tax has escaped assessment.

RULING

The SC upheld the decisions of the HCs that the section 148A shall be applicable on every Notice issued under section 148 of the ITA post April 1, 2021. It observed that the Revenue erred in issuing the impugned notices under the unamended provision when they should have been issued as per the substituted provisions introduced through the Finance Act 2021.

However, the SC denied to quash the notices and thus sustained their validity. The SC remarked that

the Revenue made a bona fide mistake to issue these notices under section 148 of the ITA because of the notifications published under the Relaxation Act 2020. It observed that there was a genuine nonapplication of the amendments as the officers of the Revenue may have been under a bona fide relief that the amendments may not yet have been enforced. Therefore, the Revenue cannot be rendered remediless and all the notices cannot be quashed or set aside because of this genuine mistake.

Therefore, to balance the interests of the Revenue and the taxpayers, the notices issued under erstwhile section 148 of the ITA shall be deemed to have been issued under section 148A of the ITA and be treated as Show Cause Notice as per section 148A(b). Further the Revenue will be obliged to comply with all the procedural requirements laid down in amended section 147 to 151 of the ITA.

The SC, thus, adjudicated that-

1. The Notices issued under section 148 of the ITA shall be deemed to be issued under section 148A of the ITA and shall be treated as Show Cause Notice under section 148A(b).

2. The AO will have 30 days from the date of the order to provide to the assessee all the information and material relied upon by the Revenue, so that the assessee can reply within 2 weeks.

3. As a one-time measure, the requirement of conducting enquiry with the prior approval of the specified authority shall be done away with in all the cases where Notices were issued post April 1, 2021.

4. All the defences and safeguards provided through amendment in section 147 to 151 shall be available to the assesses. All other legal rights will also be available with the assesses.

5. The AO shall pass the order under section 148A(d) of the ITA after following the due procedure laid down in section 148A(b) of the ITA.

ANALYSIS

The SC has passed a landmark ruling by virtue of which all the pending and closed matters including those which were closed by the HCs by quashing the Notices will be reopened. However, the SC has left multiple issues unaddressed which require consideration.

- Application of law against limitation period: With the Finance Act, 2021 reducing the limitation period for issuing notices, the deeming of notices to be issued under Section 148A of the ITA will result in notices being issued even after the expiry of the limitation period. This is because Notices relating to tax years falling within the 6-year period from March 31, 2021 which would have been otherwise been valid as per the previous law now as per the amended law stand frustrated because of the breach of limitation period of 3 years. The SC has applied the new provisions of law while ignoring the amended limitation period resulting in retroactive application of the law.

- Ignorance of law cannot be an excuse: It is a well-accepted legal principle that ignorance of law cannot be an excuse for violating it. No party can claim excuse for breach of law or inaction due to ignorance of law. The SC while in principle agreeing with the HCs has opined

that the Revenue must not have been aware of the applicability and enforceability of the amended provisions and therefore proceeded to issue Notices under un-amended section 148 of the ITA. In this respect, it should be noted that the Finance Bill, 2021 which carried the amendments that were being made to the said provisions was already tabled in Parliament and was due to be passed. To claim that the Revenue was not aware would not be a correct statement as the Finance Bill 2021 would have been passed and the provisions would have come into effect. However, the SC has condoned this ignorance has allowed the Revenue plea. This raises an important question – will this judgment stand as precedent to state that ignorance of law is a valid defence? What is the threshold when ignorance of law can be pleaded as a valid defence? This could have far reaching implications and may even be misused.

- Use of plenary powers under Article 142 of the Constitution of India: The SC employed its plenary power vested under Article 142 of the Constitution of India[4]. The use of extraordinary power to pass any order or decree as necessary for complete justice under Article 142 is only in larger public interest to provide relief specially when the statute fails to settle the dispute. Usage of powers under Article 142 for tax matters is rare and use of this power to benefit the wrong does (the Revenue in the present case) is almost never heard of. In fact, in the present case the SC first holds that the judgments of the High Courts were legal and valid, then turns around and says that because it causes prejudices to the Revenue and that 90,000 notices would be quashed, it would invoke Article 142, to validate, what it held as, illegal notices is quite disturbing and arbitrary. Article 142 does not lay down any conditions to be satisfied before such power is exercised by the SC. The exercise of power under Article 142 is left completely to the discretion of the highest court, however, extraordinary care and caution has to be observed which exercising this jurisdiction.[5] Various grounds including powers of delegated authority were raised by the assesses which were also upheld by HCs but the SC has not considered any of them in its ruling. The SC has merely considered the interest of the Revenue and has not provided why the interest of the Revenue should be safe-guarded when an error was made in their part in the first instance. While it is settled law that the directions under Article 142 are issued to do proper justice and exercise of such power cannot be considered as law laid down by SC under Article 141 of the Constitution of India[6], this judgement sets a bad precedents for the usage of power under Article 142 of the Constitution of India by the SC (in favour of revenue) especially in taxation matters.

- Need for a trust-based taxation system: The SC appreciated the Parliament for introducing the amendments in section 147 to 151 of the ITA through Finance Act 2021 to bring certainty, transparency and ease in tax administration. The SC considered that with introduction of section 148A, the process will be streamlined and the interest of the assesses will be protected as they will be vested with multiple rights including opportunity of being heard. However, now Revenue will be authorised to proceed with 90,000 Notices, which will be governed by the amended provisions of ITA. In this regard as per section 148A, the Revenue will have to provide information on the basis of which the assessment is reopened to the assessee and provide opportunity of being heard within 30 days. Further, since the impugned Notices are now deemed to be passed under section 148A of the ITA, Revenue will have to pass separate orders under section 148A(d) of the ITA in each case. Therefore, if the orders will be passed without following the due procedure, or be against the principle of natural justice or in way violative of sections 147 to 151 of the ITA, assessee will have right to challenge them. This will lead to confusion, ambiguity, unnecessary litigation and uncertainly thus axiomatically, frustrating the objectives of the provisions.
  Judgments like these lead to more uncertainty when certainty in tax matters is the need of the

hour. There is a growing need for a trust-based taxation system – a system which can be relied on, a system which does not make tax payers weary, a system that can be held accountable. This judgment will have widespread impact on both the Revenue and assesses and ripple effect for future cases. Nonetheless, it will be interesting to see how Revenue proceeds with these 90,000 cases and adjudicate the same in time bound manner.

ENDNOTES

1. Union of India v. Ashish Agarwal, Civil Appeal No. 3005/2022

2. Allahabad HC in Ashok Kumar Agarwal v. Union of India; Delhi HC in Mon Mohan Kohli v. ACIT; Calcutta HC in Bagaria Properties and Investment Private Ltd. v. Union of India; amongst others have ruled in the favour of assessee.

3. (2003) 1 SCC 72

4. Article 142 of the Constitution of India allows the Supreme Court to pass any judgement or decree in the exercise of its jurisdiction so as may be necessary to do complete justice in any case pending before it.

5. Hitesh Bhatnagar v Deepa Bhatnagar (2011) 5 SCC 234 (242): AIR 2011 SC 1637

6. State of Punjab v Rafiq Masih (2014) 8 SCC 883

National Law Review, Volume XII, Number 161