

R.M. AMBERKAR
(Private Secretary)

**IN THE HIGH COURT OF JUDICATURE AT BOMBAY
O.O.C.J.**

**INCOME TAX APPEAL NO. 1329 OF 2017
WITH
INCOME TAX APPEAL NO. 1188 OF 2017
WITH
INCOME TAX APPEAL NO. 1321 OF 2017**

Pr. Commissioner of Income Tax-1 .. Appellant
Vs
Vilson Particle Board Industries Ltd .. Respondent

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- Mr. M.N. Singh for the Appellant
 - Mr. P.J. Pardiwala, Sr. Advocate a/w Ms. Aarti Sathe for the Respondent
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**CORAM : UJJAL BHUYAN &
MILIND N. JADHAV, JJ.**

DATE : JANUARY 27, 2020.

ORAL ORDER [Per Ujjal Bhuyan, J.] :

1. This order will dispose of Income Tax Appeal Nos. 1188 of 2017, 1321 of 2017 and 1329 of 2017 as the issue arising in all these appeals is identical.

2. Heard Mr. M.N. Singh., learned standing counsel, revenue for the appellant and Mr. Pardiwala learned senior counsel along with Ms. Aarti Sathe, learned counsel for the respondent - assessee.

3. Income Tax Appeal No. 1329 of 2017 pertains to assessment year 2005-06, Income Tax Appeal No. 1188 of 2017 pertains to assessment year 2006-07 and Income Tax Appeal No. 1321 of 2017 pertains to assessment year 2007-08. However, for the sake of convenience, we take up Income Tax Appeal No. 1329 of 2017 as the lead appeal.

4. This appeal under Section 260A of the Income Tax Act, 1961 ("**the Act**" for short) is directed against the order dated 21.12.2016 passed by the Income Tax Appellate Tribunal, Pune Bench "A", Pune ("**Tribunal**" for short) in Income Tax Appeal Nos. 448/PN/2013 and 309/PN/2013 for the assessment year 2005-06.

5. Though a number of questions have been proposed by the revenue, we feel that the following two questions cover the controversy in question:-

- (A) Whether on the facts and in the circumstances of the case and in law, Tribunal was justified in treating the assessment order as bad in law by holding that reasonable opportunity of being heard should have been allowed by the Assessing Officer at pre-decisional stage, considering the mandate of Section 142(2A) of the Income Tax Act, 1961?

- (B) Whether on the facts and in the circumstances of the case and in law, Tribunal was right in holding that opportunity of being heard has to be given by the Assessing Officer and opportunity of being heard given by the superior authority i.e Commissioner of Income Tax (Central) does not constitute sufficient compliance with the rules of *audit alterm parterm*?

6. Question for consideration is as to whether the Assessing Officer is required to provide reasonable opportunity of hearing to the assessee before sending proposal for special audit under Section 142(2A) of the Act and whether the Tribunal was justified in holding so, thereafter declaring the assessment order to be invalid.

7. Facts giving rise to the present appeal have been summed up in paragraphs 38 and 39 of the Tribunal's order which we extract herein for ready reference:-

"38. Now, coming to the facts of the present case, search and seizure on the premises of group concerns was carried out on 23.08.2006. As per proviso to section 153B of the Act, the assessment proceedings in such case had to be completed by 31.12.2008, whereas the assessment order in the present case was passed on 11.06.2009. The Revenue emphasized that the assessment order passed in the case is within time frame as reference was made for special audit and time allowed for getting the special audit under section 142(2A) of the Act is to be excluded for working out the limitation period for passing the assessment order. In

this regard, the communication and correspondence before permission given to special audit need to be looked into. The learned Departmental Representative for the Revenue has filed on record copy of order sheet entries, wherein the assessee was asked to file English translation of the seized note books after assignment of case upon the DCIT, Central Circle, the order sheet entry is dated 16.05.2008. Thereafter, there was proposal to centralize Patel group cases with Addl. CIT, Circle-1, Pune. Vide order sheet entry dated 11.09.2008 itself, a proposal for audit under section 142(2A) of the Act in the case of Patel was submitted to CIT, Central, Pune through proper channel. The cases of Patel group were assigned to the ITO, Central-I, Pune on 13.10.2008. On 22.10.2008, a proposal for audit under section 142(2A) of the Act in the case of Patel group was submitted to CIT(C), Pune through proper channel. Thereafter, letter dated 21.11.2008 in respect of special audit under section 142(2A) of the Act was served upon the assessee as per order sheet entry dated 25.11.2008. On 16.12.2008, the Counsel filed a letter requesting for copies of seized note books and diaries which were supplied to him on 17.12.2008. On 30.03.2009, the cases were assigned to ITO, Central, Kolhapur and the records were handed over on 17.04.2009. Thereafter, the assessment proceedings were taken.

39. The first communication of Assessing Officer to the assessee is vide letter dated 21.11.2008, under which reference is made to the CIT (Central), Pune's order granting approval under section 142(2A) of the Act dated 01.11.2008, wherein the assessee was asked to get the accounts audited through nominated auditor within period of sixty days and submit the audited accounts along with audit report. He was also asked to get additional particulars as verified by the nominated auditor and submit the same; copy of the said letter is placed at pages 251 to 252 of the Paper Book. The assessee has

also placed on record the order granting permission under section 142(2A) of the Act by the CIT (Central), Pune which is dated 04.11.2008, under which it is mentioned that proposal dated 11.09.2008 for conducting special audit in the group cases of Patel group was received. The detailed reasons for special audit as given in the proposal are mentioned which were forwarded to the Addl. CIT, Pune. Further, show cause notice was issued to the assessee on 12.09.2008 by the CIT and he was asked to explain as to why special audit should not be ordered. The CIT in the said order mentions that along with notice of hearing, detailed proposal as received from the DCIT, Central, Kolhapur was also enclosed. The assessee was again sent another show cause notice and the assessee appeared thereafter. The CIT(C) noted that notices were inadvertently issued for compulsory audit for assessment year 2008-09 while the cases to be audited were for assessment years 2001-02 to 2007-08, hence, therefore, notices were issued to the assessee and the CIT passed the order granting permission for special audit under section 142(2A) of the Act recording the reasons for the same. The said order is placed at pages 267 to 273 of the Paper Book. The assessee has also enclosed various notices received from CIT(C) and the replies filed therein at pages 274 to 285 of the Paper Book. Thereafter, special auditor was appointed and he conducted the special audit."

7.1. Thus, from the recital of facts as extracted above, what is discernible is that the Assessing Officer had submitted a proposal for special audit under Section 142(2A) of the Act to the administrative Commissioner on 22.10.2008. Pursuant thereto, the administrative Commissioner granted approval on 4.11.2008.

8. Tribunal posed a question to itself as to whether the Assessing Officer before sending a proposal for conducting special audit under Section 142(2A) of the Act, was required to provide an opportunity of hearing to the assessee and in absence of the same, can the proceedings conducted thereafter be held to be vitiated in law. Tribunal answered the question in the following manner:-

"40. The question which arises for adjudication before us is that in the present set of facts, where the Assessing Officer before sending a proposal for conducting special audit under section 142(2A) of the Act has not given an opportunity of being heard to the assessee and in view of the proviso to section 142(2A) of the Act, is the said proposal made without affording pre-decisional hearing to the assessee valid and can the proceedings conducted thereafter be held to be vitiated in law. The Hon'ble Supreme Court in Three Judge decision in Sahara India (Firm) Vs. CIT and Another (supra) had decided the issue of show cause notice to be given on pre-decisional stage and post-decisional stage of starting the proceedings under section 142(2A) of the Act and had also referred to the earlier decision of Apex Court in Rajesh Kumar and Others Vs. DCIT (supra). The principles laid down by the Hon'ble Supreme Court are that the principle of audi alteram partem cannot be ignored even at the stage of pre-decisional hearing. In other words, in case the Assessing Officer is of the view that having regard to the nature and complexity of the accounts and interests of revenue, it is necessary to get the accounts audited by an accountant, with previous approval of Principal Chief Commissioner, then he can do so. However, the proviso inserted by the Finance Act, 2007 w.e.f. 01.06.2007 has very

categorically provided that the Assessing Officer shall not direct the assessee to get the accounts so audited unless the assessee has been given an opportunity of being heard. In other words, the principles of natural justice that a person could not be condemned unheard, have been incorporated in section itself w.e.f. 01.06.2007. The Apex Court in *Rajesh Kumar and Others Vs. DCIT (supra)* had deliberated on the provisions of the Act before insertion of said proviso but had laid down the proposition that nobody could be unheard even at the stage of forming an opinion that in view of the nature and complexity of accounts and interest of revenue, special audit is to be conducted under section 142(2A) of the Act. The Apex Court in *Sahara India (Firm) Vs. CIT and Another (supra)* have upheld the said proposition laid down by the Hon'ble Supreme Court and has also taken note of the amendment w.e.f. 01.06.2007 and have held that the principles of natural justice have to be fulfilled even at the pre-decisional stage. In conclusion, the Apex Court directed that the said proposition would be applicable prospectively. The case of the assessee before us relates to the period which is prospective to the decision of the Apex Court and is also after insertion by the Finance Act, 2007 w.e.f. 01.06.2007. Reasonable opportunity of being heard on pre-decisional stage to be allowed by the Assessing Officer to the assessee was on Statute when the proceedings were taken up against the assessee. However, as the facts reveal before submitting the proposal dated 11.09.2008 for conducting special audit under section 142(2A) of the Act to the CIT(C), no opportunity of hearing was given to the assessee. The requirement of the Act is that the Assessing Officer has to give finding that there is complexity of accounts and the interests of revenue would be affected, and in such circumstances, show cause notice needs to be given to the assessee to explain its case. Where the assessee was able to explain the nature of entries and also justify that the same are not complex, then there is no need to put

the assessee to such hardship of conducting special audit. The Assessing Officer having failed to give any opportunity of hearing to the assessee before making the proposal for conducting special audit under section 142(2A) of the Act at the pre-decisional stage, then such proposal made by the Assessing Officer to the CIT(C), Pune is against the principles of natural justice and suffers from infirmity. The case of Revenue before us is that the CIT(C), Pune before passing his order of giving permission to the Assessing Officer to ask the assessee to get the special audit conducted had given fair opportunity of hearing to the assessee. The role of CIT(C) is the role of approving authority. The role is not that of adjudicating authority which had to be carried out by the Assessing Officer. The adjudicating authority in the present set of facts has failed to give any opportunity to the assessee before making proposal for special audit and the opportunity allowed by the approving authority, who in any case is enshrined with the duties of checking whether there is no arbitrariness in functioning of adjudicating authority, has to be satisfied before giving approval. Hence, the opportunity allowed by the CIT(C), Pune after proposal was made by the adjudicating authority does not absolve the non-allowance of reasonable opportunity of hearing by the Assessing Officer.

41. Applying the principles laid down by the Apex Court in Sahara India (Firm) Vs. CIT and Another (supra), we hold that where no show cause notice was given to the assessee before making the order proposing conduct of special audit under section 142(2A) of the Act, in the present case and the CIT having approved the said proposal though after giving opportunity of hearing to the assessee is vitiated because of non-compliance with the principles of natural justice. Accordingly, the assessment order passed in the facts of present case is beyond the period of limitation and hence, the same is invalid and bad in law."

8.1. Thus, Tribunal held that show cause notice was required to be given to the assessee by the Assessing Officer before making the order proposing conduct of special audit under Section 142(2A) of the Act and even if the administrative Commissioner approves the said proposal after giving opportunity to the assessee, nonetheless such a course of action would be vitiated because of non-compliance to the principles of natural justice at the stage of making the proposal. Accordingly, Tribunal interfered with the same. It may also be mentioned that following setting aside of the approval given by the administrative Commissioner, the assessment order in the present case (following search) was found to be beyond the period of limitation. Therefore, the same was declared invalid and bad in law.

9. At this stage, we may advert to Section 142(2A) of the Act. Section 142 deals with inquiry before assessment. Sub-section (2A) as it existed prior to the Finance Act,2007 reads as under:-

"(2A) If, at any stage of the proceedings before him, the Assessing Officer, having regard to the nature and complexity of the accounts, volume of the accounts, doubts about the correctness of the

accounts, multiplicity of transactions in the accounts or specialised nature of business activity of the assessee, and the interests of the revenue, is of the opinion that it is necessary so to do, he may, with the previous approval of the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner, direct the assessee to get the accounts audited by an accountant, as defined in the Explanation below sub-section (2) of section 288, nominated by the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner in this behalf and to furnish a report of such audit in the prescribed form duly signed and verified by such accountant and setting forth such particulars as may be prescribed and such other particulars as the Assessing Officer may require."

9.1. Thus, sub-section (2A) of Section 142 provides that in the course of the assessment proceedings, if the Assessing Officer forms an opinion that the accounts of the assessee is required to be audited by an accountant as defined under the Act as the accounts are complex, voluminous, questionable etc and in the interest of the revenue, he may direct the assessee to get the accounts audited by such accountant and to furnish report of such audit, subject to previous approval of the higher authority as mentioned.

10. In **Rajesh Kumar Vs. Deputy CIT**¹, Supreme Court was confronted with the question as to whether before a

¹ [2006] 287 ITR 91 (SC)

proposal for special audit under Section 142(2A) of the Act was made, was there a requirement of providing pre-decisional hearing to the assessee. Supreme Court took the view that an order of directing special audit entails civil consequences and therefore, principles of natural justice was held to be implicit under Section 142(2A) of the Act. Thus, there is requirement of providing pre-decisional hearing by the Assessing Officer to the assessee before forming opinion to submit proposal for special audit. In the said case, Supreme Court also held that an order of approval by the higher authority is also not to be mechanically granted. The same should be done having regard to the materials on record and considering the explanation given by the assessee.

11. Thus, in Rajesh Kumar (supra), Supreme Court read into Section 142(2A) of the Act principles of natural justice and held that before forming an opinion as to the need for a special audit, having regard to the requirement of Section 142(2A), a pre-decisional hearing has to be given by the Assessing Officer to the assessee. Even thereafter when the

question of approval is before the approving authority, the latter is also required to comply with the principles of natural justice. Therefore, in both the stages contemplated under Section 142(2A), principles of natural justice are required to be followed.

12. The above decision of the Supreme Court in Rajesh Kumar (supra) was referred to a larger bench and was examined in **Sahara India (Firm) Vs. Commissioner of Income Tax²**. In Sahara India (supra), the larger bench of the Supreme Court agreed with the decision in Rajesh Kumar (supra).

13. It may also be noted that in the meanwhile, by the Finance Act, 2007 w.e.f. 1.6.2007, the following proviso was added to Section 142(2A) of the Act:-

"Provided that the Assessing Officer shall not direct the assessee to get the accounts so audited unless the assessee has been given a reasonable opportunity of being heard."

13.1 Therefore, following the amendment, it is now a statutory requirement that the Assessing Officer has to

² [2008] 300 ITR 403 (SC)

provide reasonable opportunity of hearing to the assessee before directing the assessee to get the accounts audited under the said provision.

14. Reverting back to Sahara India (supra), Supreme Court held that special audit is more or less in the nature of an investigation and in some cases, may even turn out to be stigmatic. Therefore, even after the obligation to pay the auditor's fees by the assessee, civil consequences would still ensue on the passing of an order for special audit. Finally, Supreme Court held as under:-

"24. The upshot of the entire discussion is that the exercise of power under section 142(2A) of the Act leads to serious civil consequences and, therefore, even in the absence of express provision for affording an opportunity of pre-decisional hearing to an assessee and in the absence of any express provision in Section 142(2A) barring the giving of reasonable opportunity to an assessee, the requirement of observance of principles of natural justice is to be read into the said provision. Accordingly, we reiterate the view expressed in Rajesh Kumar's case (supra).

25. It is pertinent to note that by the Finance Act, 2007, a proviso to Section (2A) has been inserted with effect from June 1, 2007, which provides that no direction for special audit shall be issued without affording a reasonable opportunity of hearing to the assessee."

14.1 In the light of the legal position as above, we have no hesitation in holding that in the absence of pre-decisional hearing, the decision to have special audit was invalid and consequentially, all the proceedings conducted thereafter stood vitiated.

15. There is no error or infirmity in the order passed by the Tribunal. No substantial question of law arises from the aforesaid order of the Tribunal. Appeal is devoid of any merit and is accordingly dismissed.

16. This order will also cover the other two appeals i.e Income Tax Appeal Nos. 1188 of 2017 and 1329 of 2017. Accordingly, both these appeals are dismissed.

[MILIND N. JADHAV, J.]

[UJJAL BHUYAN, J.]