**IN THE HIGH COURT AT CALCUTTA**
**Special Jurisdiction (Income-Tax)**
**(Original Side)**

**Present:**
**The Hon'ble Mr. Justice Bhaskar Bhattacharya**
**And**
**The Hon'ble Mr. Justice Sambuddha Chakrabarti**

**I.T.A. No.224 of 2004**

**Bhartia Industries Limited**

**Versus**

**Commissioner of Income-Tax, Central-III**

For the Appellant: Mr. R.N. Bajoria,
Mr. J.P. Khaitan,
Mr. S. Das,
Mr. C.S. Das.

For the Respondent: Mr. R.N. Bandopadhya,
Ms. Susmita Das De.

Heard on. 16.06.2011

Judgment on: August 2, 2011.

**Bhaskar Bhattacharya, J.:**

This appeal under Section 260A of the Income-tax Act, 1961 ("Act") is at the instance of an assessee and is directed against an order dated March 3, 2004 passed by the Income-tax Appellate Tribunal, "C" Bench, Kolkata in ITA No.867 (kol) of 2002 for the Assessment Year 1998-99, dismissing the appeal filed by the assessee against an order dated March 4, 2003 passed under Section 263 of the Act.

Being dissatisfied, the assessee has come up with the present appeal.

The facts giving rise to filing of the present appeal may be summarized thus:

a) The appellant is, *inter alia,* engaged in the business of manufacturing electrical equipments and is assessed to tax under the provision of the Act. The present appeal relates to the appellant's assessment for the Assessment Year 1998-99 the relevant previous year being the year ended on March 31, 1998.

b) The appellant claimed that it had large number of surplus employees which was affecting its economical day-to-day working and causing financial hardship and as a result, the appellant framed a Voluntary Retirement Scheme giving an option to its employees to seek voluntary retirement between October 15, 1996 and March 31, 1997. The said option to seek the voluntary retirement was later extended till October, 1997.

c) The VRS Scheme was duly approved by the Director General of Income-tax (Investigation) under Section 10(10C) of the Act and Rule 2BA of the Income-tax Rules, 1962. In terms of the said VRS Scheme the appellant incurred an expenditure of 3,38,09,825/- during the relevant previous year for the Assessment Year 1998-99 and the said

sum was claimed by the appellant in its return filed for the Assessment Year 1998-99 as a revenue expenditure.

d) The Assessing Officer in course of the assessment proceedings obtained full details of the said expenditure incurred on account of VRS and after considering all the facts and circumstances allowed deduction for the same.

e) Subsequently, the Commissioner of Income-tax initiated proceedings under Section 263 of the Act questioning the allowance of the said payments made on account of VRS by the Assessing Officer and an order under Section 263 of the Act dated March 4, 2003 was passed by the Commissioner under Section 263 of the Act. In the said order the Commissioner observed that the Assessing Officer was bound by the Circular dated January 23, 2001 issued by the Board as to the eligibility of deduction of such payment on account of VRS and he should not have allowed such payment. The Commissioner set aside the entire assessment for being made de novo and directed the Assessing Officer to make fresh assessment in the light of the said Circular of the Board.

f) Being dissatisfied, the appellant preferred an appeal before the Income-tax Appellate Tribunal and by the order impugned herein the said Tribunal has affirmed the order passed by the Commissioner under Section 263 of the Act. The Tribunal held that the Assessing

Officer was duty bound to follow the instruction of the Central Board of Direct Taxes and non-compliance of such instructions amounted to dereliction of duty and subordination.

g) Being dissatisfied, the appellant has come up with the present appeal.

A Division Bench of this Court at the time of admission of this appeal formulated the following substantial question of law:

"a) Whether the Tribunal was justified in law in holding that the said circular dated January 23, 2001 was binding on the Assessing Officer in the assessment proceedings before him?

"b) Whether the Board had any jurisdiction, power or authority to issue any instructions or order in relation to the quasi judicial functions of the Assessing Officer in the assessment proceedings?

"c) Whether the instructions of the board as contained in the said circular dated January 23, 2001 are contrary to law in holding that the payments made on account of VRS are not allowable revenue expenditure?

"d) Whether the Tribunal was justified in holding the order of the Commissioner setting aside the entire assessment and directing a

fresh assessment de novo when admittedly on none of the other issues there was any controversy?

"e) Whether jurisdiction under Section 263 of the Act could be assumed in the facts and circumstances of the case by the Commissioner when the Assessing Office had taken a reasonable and possible view in allowing the deduction in respect of the said payments on account of VRS?"

Mr. Bajoria, the learned Senior Advocate appearing on behalf of the appellant, has criticized the order of the Tribunal by pointing out that the Tribunal below did not consider the scope of Section 263 of the Act which did not authorize reopening of the assessment merely because of the existence of a Circular issued under Section 119 of the Act taking a contrary view on the subject-matter of the assessment. According to Mr. Bajoria, the said Circular dated 23rd January, 2001 was on the face of it against the spirit of Section 119 of the Act inasmuch as no Circular could be issued for guiding the Assessing Officer for assessment which is a quasi judicial duty of the officer concerned. Mr. Bajoria, therefore, contends that the said Circular being issued in violation of the provision contained in Section 119 of the Act, on that basis, the assessment could not be reopened.

Mr. Bajoria next contends that it is the consistent view of different High Courts that the expenditure made pursuant to any scheme of voluntary

retirement for the purpose of smooth running of the business amounts to revenue expenditure and as such, there was no justification of reopening the transaction on the basis of a Circular which guided the Assessing Officer to treat the amount spent pursuant to such scheme as capital expenditure.

Mr. Bajoria further contends that where conflicting views are possible on the question of interpretation of the provisions of the Act, there is no scope of invocation of Section 263 of the Act and thus, on that ground alone, the order passed by the Commissioner of Income-tax and the Tribunal should be set aside. In support of such contention, Mr. Bajoria relied upon the following decisions:

1. Grindlays Bank P.L.C. vs. Commissioner of Income-Tax, reported in 1993 Vol.201 ITR 148;

2. Commissioner of Income-Tax vs. Machinery Manufacturing Corporation Ltd., reported in 1992 Vol.198 ITR 559;

3. Malabar Industrial Co. Ltd. vs. Commissioner of Income-Tax, reported in 2000 Vol.243 ITR 83;

4. Commissioner of Income-tax, Cochin vs. O E N India Ltd., reported in 2011 Vol.196 ITR 131;

5. Commissioner of Income-tax vs. Bhor Industries Ltd., reported in 2003 Vol.264 ITR 180;

6. Empire Jute Co. Ltd. vs. Commissioner of Income-Tax, reported in 1980 Vol.124 ITR 1;

7. Sassoon J. David & Co. P. Ltd. vs. Commissioner of Income-tax, Bombay, reported in 1979 Vol.261 ITR 118.

Mr. Banerjee, the learned Advocate appearing on behalf of the Revenue, has, on the other hand, opposed the aforesaid contentions of Mr. Bajoria and has contended that the Circular dated 23rd January, 2001 was very much binding upon the Assessing Officer and as such, the Commissioner of Income-tax (Appeals) rightly initiated a proceeding under Section 263 of the Act for reopening of the assessment in accordance with the direction given in the said Circular. Mr. Banerjee submits that the direction contained in Circular are in conformity with the decisions of the Supreme Court and as such, there is no illegality in the order impugned in this appeal. Mr. Banerjee, therefore, prays for dismissal of this appeal.

In order to appreciate the questions involved in this appeal, first we propose to consider the scope of Section 119 of the Act which is quoted below:

> ***119. Instructions to subordinate authorities****.—(1) The Board may, from time to time, issue such orders, instructions and directions to other Income Tax authorities as it may deem fit for the proper administration of this Act, and such authorities and all other persons employed in the execution of this Act shall observe and follow such orders, instructions and directions of the Board:*

***Provided that no such orders, instructions or directions shall be issued—***

***(a) so as to require any Income Tax authority to make a particular assessment or to dispose of a particular case in a particular manner; or***

***(b) so as to interfere with the discretion of the [1][* * *] Commissioner (Appeals) in the exercise of his appellate functions.***

*(2) Without prejudice to the generality of the foregoing power,—*

*(a) the Board may, if it considers it necessary or expedient so to do, for the purpose of proper and efficient management of the work of assessment and collection of revenue, issue, from time to time (whether by way of relaxation of any of the provisions of Sections [2][115-P, 115-S,][3][, 115-WD, 115-WE, 115-WF, 115-WG, 115-WH, 115-WJ, 115-WK][4][139,] 143, 144, 147, 148, 154, 155 [5][, 158-BFA], [6][sub-section (1-A) of Section 201, Sections 210, 211, 234-A, 234-B, 234-C,] 271 and 273 or otherwise), general or special orders in respect of any class of incomes [7][or fringe benefits] or class of cases, setting forth directions or instructions (not being prejudicial to assessees) as to the guidelines, principles or procedures to be followed by other Income Tax authorities in the work relating to assessment or collection of revenue or the initiation of proceedings for the imposition of penalties and any such order may, if the Board is of opinion that it is necessary in the public interest so to do, be published and circulated in the prescribed manner for general information;*

*(b) the Board may, if it considers it desirable or expedient so to do for avoiding genuine hardship in any case or class of cases, by general or special order, authorise any Income Tax authority, not being a [* * *] Commissioner (Appeals) to admit an application or claim for any*

*exemption, deduction, refund or any other relief under this Act after the expiry of the period specified by or under this Act for making such application or claim and deal with the same on merits in accordance with law;*

*(c) the Board may, if it considers it desirable or expedient so to do for avoiding genuine hardship in any case or class of cases, by general or special order for reasons to be specified therein, relax any requirement contained in any of the provisions of Chapter IV or Chapter VI-A, where the assessee has failed to comply with any requirement specified in such provision for claiming deduction thereunder, subject to the following conditions, namely:—*

*(i) the default in complying with such requirement was due to circumstances beyond the control of the assessee; and*

*(ii) the assessee has complied with such requirement before the completion of assessment in relation to the previous year in which such deduction is claimed:*

***Provided** that the Central Government shall cause every order issued under this clause to be laid before each House of Parliament.*

(Emphasis supplied by us).

On a plain reading of the said provision, we have no doubt in our mind that the circular issued by the Board under the aforesaid provision is meant for guiding the officers of the Revenue for administrative purpose of enforcing the provisions of the Act. But when an authority under the Act is required to perform quasi-judicial functions, such authorities should be guided by the law of the land as enunciated on the questions involved by various judicial authorities which have binding effect. If an existing circular is in conflict with the law of the land

laid down by the High Courts or the Supreme Court, in our view, the Revenue Authorities, while acting quasi judicially, should ignore such circulars in discharge of their quasi-judicial functions.

In this connection, we are fortified by the following observations of the Supreme Court in the case of M/s. Hindustan Aeronautics Ltd., Bangalore vs. Commissioner of Income-tax, Karnataka-I, Bangalore, reported in AIR 2000 SC 2178, while considering the effect of a circular on a judicial decision taking a contrary view:

> *"However, the learned counsel for the appellant relied on the decisions in Navnitlal C. Javeri v. K.K. Sen, AAC of Income-tax 56 ITR 198 : (AIR 1965 SC 1375); Ellerman Lines Ltd. v. C.I.T., 82 ITR 913 : (AIR 1972 SC 524 : 1972 Tax LR 246) and K.P. Varghese v. ITO, 131 ITR 509 : (AIR 1981 SC 1922 : 1981 Tax LR 1448) to contend that the circular issued by the Board under Section 119 of the Act is binding on the Commissioner in terms of which he was bound to examine the revision of the appellant on merits and the order of the learned single Judge merely gives effect to such a course. Dr. Gauri Shankar learned senior advocate for the Revenue, however,* ***pointed out by referring to several decisions of this Court to the effect that the circulars or instructions given by the Board are no doubt binding in law on the authorities under the Act but when the Supreme Court or the High Court has declared the law on the question arising for consideration it will not be open to a Court to direct that a circular should be given effect to and not the view expressed in a decision of the Supreme Court or the High Court. We find***

> ***great force in this submission made by the learned senior advocate for the Revenue*** *and find absolutely no merit in this appeal and the same stands dismissed, but in the circumstances of the case, there shall be no orders as to costs."*
>
> (Emphasis given by us).

Earlier, in the case of UCO Bank Ltd. vs. CIT, reported in AIR 1999 SC 2082, a three-judge-bench of the Supreme Court made the following observations about the effect of a circular issued under Section 119 of the Act:

> *"What is the status of these circulars? Section 119(1) of the Income-tax Act, 1961 provides that, "The Central Board of Direct Taxes may, from time to time, issue such orders, instructions and directions to other Income-tax authorities as it may deem fit for the proper administration of this Act and such authorities and all other persons employed in the execution of this Act shall observe and follow such orders, instructions and directions of the Board. Provided that no such orders, instructions or directions shall be issued (a) so as to require any Income-tax authority to make a particular assessment or to dispose of a particular case in a particular manner: or (b) so as to interfere with the discretion of the Appellate Assistant Commissioner in the exercise of his appellate functions." Under sub-section (2) of Section 119 without prejudice to the generality of the Board's power set out in sub-section (1) a specific power is given to the Board for the purpose of proper and efficient management of the work of assessment and collection of revenue to issue from time to time general or special orders in respect of any class of incomes or class of cases setting forth directions or instructions, not being prejudicial to assessees, as the guidelines, principles or procedures to be*

*followed in the work relating to assessment. Such instructions may be by way of relaxation of any of the provisions of the sections specified there or otherwise. The Board thus has power, inter alia, to tone down the rigour of the law and ensure a fair enforcement of its provisions, by issuing circulars in exercise of its statutory powers under Section 119 of the Income-tax Act which are binding on the authorities in the administration of the Act. Under Section 119(2)(a) however, the circulars as contemplated therein cannot be adverse to the assessee. Thus, the authority which wields the power for its own advantage under the Act is given the right to forego the advantage when required to wield it in a manner it considers just by relaxing the rigour of the law or in other permissible manners as laid down in Section 119. The power is given for the purpose of just, proper and efficient management of the work of assessment and in public interest. It is a beneficial power given to the Board for proper administration of fiscal law so that undue hardship may not be caused to the assessee and the fiscal laws may be correctly applied. Hard cases which can be properly categorised as belonging to a class, can thus be given the benefit of relaxation of law by issuing circulars binding on the taxing authorities."*

In a subsequent case of five-judge-bench of the Supreme Court in the case of Collector of Central Excise, Vadodra vs. M/s. Dhiren Chemical Industries, reported in AIR 2002 SC 453, the said Bench while interpreting an exemption notification issued under the Central Excise Rules (1944) that used the phrase *"on which the appropriate amount of duty of excise has already been paid"* observed as follows;

> *"We need to make it clear that, regardless of the interpretation that we have placed on the said phrase, if there are circulars which have been issued by the Central Board of Excise and Customs which place a different interpretation upon the said phrase, that interpretation will be binding upon the Revenue."*

In a subsequent two-judge-bench in the case of Commissioner of Customs vs. Indian Oil Corporation, reported in (2004) 3 SCC 488, one of the judges, viz. Ruma Pal, J. was of the opinion that in view of the decision in the case of Dhiren Chemical Industries (supra), the earlier decision of the two-judge-bench in the case of M/s. Hindustan Aeronautics Ltd., Bangalore (supra), was not good law while the other judge of the bench, viz. P. Venkatrama Reddy, expressed doubt in the above view of Pal, J. and observed as follows:

*"As is evident from Section 151-A, the Board is empowered to issue orders or instructions in order to ensure uniformity in the classification of goods or with respect to levy of duty. The need to issue such instructions arises when there is a doubt or ambiguity in relation to those matters. The possibility of varying views being taken by the customs officials while administering the Act may bring about uncertainty and confusion. In order to avoid this situation, Section 151-A has been enacted on the same lines as Section 37-A of the Central Excise Act. The apparent need to issue such circulars is felt when there is no authoritative pronouncement of the Court on the subject. Once the relevant issue is decided by the Court at the highest level, the very basis and substratum of the circular disappears. The law laid down by this Court will ensure uniformity in the decisions at all levels. By an express constitutional provision, the law declared by the Supreme Court is made binding on all the courts within the territory of India (vide Article 141). Proprio vigore the law is binding on all the tribunals and authorities. Can it be said that even after the law is declared by the Supreme Court the adjudicating authority*

*should still give effect to the circular issued by the Board ignoring the legal position laid down by this Court? Even after the legal position is settled by the highest court of the land, should the Customs Authority continue to give primacy to the circular of the Board? Should Section 151-A be taken to such extremities? Was it enacted for such purpose? Does it not amount to transgression of constitutional mandate while adhering to a statutory mandate? Even after the reason and rationale underlying the circular disappears, is it obligatory to continue to follow the circular? These are the questions which puzzle me and these are the conclusions which follow if the observations of this Court in the two cases of Dhiren Chemical Industries are taken to their logical conclusion.*

*I am of the view that in a situation like this, the Customs Authority should obey the constitutional mandate emanating from Article 141 read with Article 144 rather than adhering to the letter of a statutory provision like Section 151-A of the Customs Act. The Customs Authority should act subservient to the decision of the highest constitutional court and not to the circular of the Board which is denuded of its rationale and substratum under the impact of the authoritative pronouncement of the highest court. Alternatively, Section 151-A has to be suitably read down so that the circulars issued would not come into conflict with the decision of this Court which the Customs Authorities are under a constitutional obligation to follow.*

> *I can perceive of no principle or authority to countenance the view expressed in Dhiren Chemical case that regardless of the interpretation placed by this Court, the circulars which give a different interpretation would still survive and they have to be necessarily followed by the statutory functionaries. The opinion expressed in the case of Hindustan Aeronautics Ltd. v. CIT seems to project a correct view, though that decision cannot prevail over the Constitution Bench decision in Dhiren Chemical Industries. The unintended results that may follow from the verdict of this Court in Dhiren Chemical Industries*

> *is another aspect that has worried me. Let us take a case where in accordance with the instructions in the circular of the Board, the adjudicating authority has to decide the case against the assessee, but as per the decision of this Court, the assessee's contention has to be accepted by the adjudicating authority. If the proposition laid down in Dhiren Chemical Industries has to be followed, the adjudicating authority should pass an order in terms of the circular holding the issue in favour of the Revenue, knowing fully well that on a challenge by the assessee, it is liable to be set aside in appeal. The assessee will then be driven to file an appeal to get rid of an obviously illegal order. Is it all contemplated by Section 151-A?*

The aforesaid observations of P. Venkatrama Reddy, J. is more convincing than the view taken by Pal, J. declaring the decision in the case of *Hindustan Aeronautics Ltd. v. CIT (supra),* as per incurium.

We respectfully follow the view taken in Hindustan Aeronautics Ltd. *(supra)* and the one taken by P. Venkatrama Reddy, J.

Applying the aforesaid principles to the facts of the present case, we find that the sole reason for invocation of Section 263 of the Act is a circular dated January 23, 2001 issued in terms of Section 119 of the Act. The outcome of the original order of assessment was in tune with the Division Bench decisions of this Court in the cases of Commissioner of Income tax vs. Machinery Manufacturing Ltd., reported in (1992) 198 ITR 559 and Grindlays Bank P.L.C vs. C.I.T, reported in (1993) 201 ITR 148 where the Division Bench in the former

case held that the payment of compensation to induce the workmen to retire prematurely is an item of expenditure incurred by the Company on the ground of commercial expediency in order to facilitate the carrying on of business and a revenue expenditure and allowable deduction and in the latter one, it was held that the entire initial contribution to staff pension fund in respect of past services of its members was deductable. The same view has been taken by the Bombay High Court and the Kerala High Court in the cases of CIT vs. Bhor Industries Ltd and CIT vs. OEN India Ltd, reported in 264 ITR 180 and (2011) 196 Taxman 131 respectively.

Thus, the Commissioner of Income tax simply by taking aid of a circular which says that *ex-gratia* payment made for gaining enduring benefit or voluntary retirement scheme should be *prima facie* treated as capital expenditure sought to reopen the assessment by invoking Section 263 of the Act notwithstanding the fact that the said circular is in conflict with the view of this High Court which is binding upon the Assessing Officer.

At this stage, it will not be out of place to mention that the test of enduring benefit is not conclusive test to determine the nature of expenditure as held by the Supreme Court in the case of Empire Jute Co. Ltd. vs. CIT, reported in AIR 1980 SC 1946 relied upon by Mr. Bajoria.

In the case of Empire Jute Co. Ltd. (supra), the assessee was a limited company carrying on business of manufacture of jute. It had a factory with a certain number of looms situate in West Bengal. It was a member of the Indian Jute Mills Association. With a view to adjusting the production of the mills to the demand in the world market, a working time agreement was entered into between the members of the Association restricting the number of working hours per week, for which the mills were entitled to work their looms. Cl. 6(a) of the agreement enabled members to be registered as a "Group of Mills" if they happened to be under the control of the same managing agents or were combined by any arrangement or agreement and it was open to any member of the Group of Mills so registered to utilize the allotment of hours of work per week of other members in the same group who were not fully utilizing the hours of work allowable to them under the working time agreement, provided that such transfer of hours of work was for a period of not less than six months. This transaction of transfer of allotment of hours of work per week was commonly referred to as sale of looms hours by one member to another. The consequence of such transfer was that the hours of work per week transferred by a member were liable to be deducted from the working hours per week allowed to such member under the working time agreement and the member in whose favour such transfer was made was entitled to utilise the number of working hours per week transferred to him in addition to the working hours per week allowed to him under the working time agreement. It was under this clause that the assessee purchased loom hours from four different jute manufacturing concerns which were signatories to

the working time agreement, for the aggregate sum of Rs. 2,03,225/- during the year 1st Aug. 1958 to 31st July 1959. In the course of assessment for the Assessment Year 1960-61 for which the relevant accounting year was the previous year 1st Aug. 1958 to 31st July 1959, the assessee claimed to deduct this amount of Rupees 2,03,255/- as revenue expenditure on the ground that it was part of the cost of operating the looms which constituted the profit making apparatus of the assessee. While dealing with such a case and holding in favour of the assessee, the Supreme Court observed as follows:

> *"The test of enduring benefit is therefore not a certain or conclusive test and it cannot be applied blindly and mechanically without regard to the particular facts and circumstances of a given case. But even if this test were applied in the present case, it does not yield a conclusion in favour of the Revenue. Here, by purchase of loom hour no new asset has been created. There is no addition to or expansion of the profit making apparatus of the assessee. The income earning machine remains what it was prior to the purchase of loom hours. The assessee is merely enabled to operate the profit making structure for a longer number of hours. And this advantage is clearly not of an enduring nature. It is limited in its duration to six months and, moreover, the additional working hours per week transferred to the assessee have to be utilised during the week and cannot be carried forward to the next week. It is, therefore, not possible to say that any advantage of enduring benefit in the capital field was acquired by the assessee in purchasing loom hours and the test of enduring benefit cannot help the Revenue."*

We, therefore, find that the authorities below committed substantial error of law in approving the reopening of the assessment on the basis of the circular referred to above and thus, we set aside the order of the Tribunal and the order passed under Section 263 of the Act.

The appeal is, thus, allowed by answering the questions formulated in this appeal in the following way:

a)- In the negative and against the Revenue.

b)- In the negative and against the Revenue.

c)- In the affirmative and against the Revenue.

d)- In the negative and against the Revenue.

e)- In the negative and against the Revenue.

In the facts and circumstances, there will be, however, no order as to costs.

**(Bhaskar Bhattacharya, J.)**

I agree.

**(Sambuddha Chakrabarti, J.)**