HIGH COURT OF MADRAS
Commissioner of Income-tax, Chennai
v.
High Energy Batteries (India) Ltd.*

MRS. CHITRA VENKATARAMAN AND
K. RAVICHANDRA BAABU, JJ.
T.C. (APPEAL) NOS. 579 TO 581 OF 2005†
APRIL 17, 2012
ORDER

Mrs. Chitra Venkataraman, J. - The Revenue is on appeal as against the order of the Tribunal, relating to the assessment years 1995-96, 1996-97 and 1997-98.

2. The following are the substantial questions of law raised in these Tax Case Appeals:

(*i*) Whether on the facts and in the circumstances of the case, the Tribunal was right in holding that the re-opening of assessment by the assessing officer for the years 1995-96 & 1996-97 was bad in law?

(*ii*) Whether on the facts and in the circumstances of the case, the Tribunal was right in holding that the assessee was entitled to depreciation?

(*iii*) Whether on the facts and in the circumstances of the case, the Tribunal was right in treating the hire purchase and the lease transactions as genuine as far as the assessee was concerned?

(*iv*) Whether on the facts and in the circumstances of the case, the Tribunal was right in permitting depreciation as claimed when the value of the asset could only be the written down value in the books of the seller as per explanation 3 to Section 43(1)?

Assessment year 1995-96 relates to the reopening of assessment under Section 147 of the Income Tax Act and the assessment for other two assessment years are under Sections 143(1)(a) and 143(3) of the Income Tax Act respectively.

3. The facts leading to the grant of depreciation and subsequent withdrawal are as follows:

The assessee herein purchased igni-fluid boiler from its sister concern M/s. Ponni Sugars Limited. It is seen from the minutes of the meeting of the Board of Directors of M/s. Ponni Sugars and Chemicals that the said company had gone for sale of the boilers to meet a portion of the cash loss and other financial commitments of the said company. It is seen from the facts herein that the total consideration for the sale of the said igni fluid boiler was Rs. 250 lakhs. The date of sale was 10.3.1995. The assessee is said to have parted with a sum of Rs. 50 lakhs and for the balance of the sale consideration, it had entered into a finance agreement with M/s. Wipro Finance Limited by way of hire purchase agreement on 10th March 1995. On the very same day, the assessee is said to have entered into an agreement of lease of the boilers with M/s. Ponni Sugars and Chemicals Limited. The Assessing Authority viewed the sale and lease back arrangement as a camouflaged one and held that the assessee was not entitled to the claim of depreciation. The reasons for viewing it so were that:

(*i*) In the hire purchase agreement, Wipro Finance Limited was shown as the owner of the asset and the assessee, a hirer.

(*ii*) The asset shown never moved out of the possession of the seller namely, M/s. Ponni Sugars and Chemicals Limited and continued to be the asset of the lessee.

(*iii*) The alleged purchase was only a financial accommodation to a sister concern as evidenced from the minutes of the meeting of the Board of Directors of M/s. Ponni Sugars and Chemicals Limited.

(*iv*) After going through all arrangements for finance, the hire purchase agreement and lease agreement were entered into.

In the circumstances, the Assessing Authority invoked its jurisdiction under Section 147 of the Income Tax Act to reopen the assessment in respect of the completed assessment for the assessment year 1995-96.

4. As far as the assessment year 1996-97 is concerned, in respect of the intimation under Section 143(1)(a) accepting the loss, proceedings under Section 148 was initiated on the very same ground as had been done for the earlier year. So too, in respect of the assessment year 1997-98, proceedings were finalised under Section 143(3) on the very same ground, on the claim of depreciation. The assessee objected to the reopening of the assessment as well as to the view taken by the Assessing Authority as to the genuineness of the transaction, which, ultimately, was rejected by the Officer.

5. Aggrieved by the assessment for the assessment year 1995-96, the assessee went on appeal before the Commissioner of Income Tax (Appeals). A perusal of the order of the Commissioner of Income Tax (Appeals) for the assessment year 1995-96 shows the finding in paragraph 1.3.4 that the said appellate authority perused the Assessing Officer's records, wherein, the note filed by the assessee as regards the claim on depreciation on the leased out property was given. The first appellate authority pointed out that in the course of the original assessment proceedings, details relating to the sale and lease back transactions were furnished and that there was nothing on record to indicate that the Assessing Officer had consciously applied his mind on the issue of allowability of depreciation and consciously took a decision to allow depreciation on the same. Thus the first appellate authority viewed that when there had been an appraisal of the facts by the Assessing Officer subsequent to assessment, it could not be considered as a change of opinion. Thus the first appellate authority rejected the claim of the assessee on the aspect of jurisdiction to reopen the assessment under Section 147 of the Income Tax Act.

6. On the question of the claim of depreciation on ignifluid boiler, the first appellate authority pointed out that the assessee is principally engaged in a high technology area of manufacture of sophisticated high voltage batteries used in missiles, air crafts, etc. The business of leasing was subsequently incorporated in the year 1990. As regards the transaction that had been put through, the first appellate authority pointed out that on the first date of its entering into the hire purchase agreement itself, by entering into a lease agreement with its sister concern, the assessee had stayed away from taking the risk of transactions with the hire purchase company. All that the assessee had paid in the sale transaction was only a sum of Rs.50.88 lakhs, but by entering into the hire purchase agreement, the assessee had got a benefit of Rs. 2.5 crores depreciation, thereby reducing its tax liability substantially. Pointing out to the two types of lease, viz., operational lease and finance leasing, the first appellate authority held that it was neither a finance lease nor an operational lease. Essentially, it was financing by M/s. Wipro Finance Limited to Ponni Sugars and Chemicals Limited. Thus the transaction by finance and leasing was only a sham and nominal transaction. The role of the assessee in the transaction had been made to appear as though it is a real transaction. On the other hand, there was no real commercial significance other than the purchase of depreciation of Rs. 2.5 crores by paying Rs.50.88

lakhs. In the above circumstances, the first appellate authority held that the Assessing Officer was well within his rights to determine the claim by lifting the veil. Thus applying the decision in *McDowell & Co. Ltd.* v. *CTO* [1985] 154 ITR 148/22 Taxman 11 (SC), the assessment was confirmed. Aggrieved by this, the assessee went on appeal before the Tribunal. Taking all the three appeals together, the Tribunal pointed out in paragraph 8.19 on the aspect of reopening of the assessment for 1995-96 that the same was only a mere change of opinion and that there were no materials at all to support the reassessment.

7. As far as the assessment year 1996-97 was concerned, on facts as regards the genuineness of the transaction, it allowed the appeals relating to the assessment years 1996-97 as well as 1997-98. The Tribunal pointed out that the Revenue had not brought on record any material to come to a conclusion that the transaction was a sham one. The Tribunal pointed out to the valuation aspect of the boiler that there was one valuation of the boiler at Rs. 2.53 crores and the deal was struck at Rs. 2.50 crores. The Tribunal pointed out that the assessee had placed the shareholdings of the two concerns which included financial institutions like I.C.I.C.I., I.D.B.I., U.T.I., apart from others. The Tribunal pointed out that when the fact relating to the sale and the subsequent financial agreement, hire purchase agreement as well as leasing transaction had all been placed before the financial institutions for their clearance and when the assessee had obtained clearance from I.C.I.C.I, for the transaction, it was difficult to come to the conclusion that the transaction was only a sham transaction to benefit the assessee. Thus the Tribunal viewed that in the absence of any material, either direct or circumstantial, to show that the transactions were sham documents, it was difficult to accept the view of the Commissioner of Income Tax (Appeals) as well as the Revenue's contention. Thus on the ground that the Revenue had failed to prove that the transaction was a colourable one, the Tribunal allowed the appeals of the assessee. Aggrieved by the same, the Revenue is on appeal before this Court.

8. As far as the reopening of the assessment for the assessment year 1995-96 is concerned, the law on the scope of Section 147 is well laid down. In the recent decision in *CIT* v. *Kelvinator of India Ltd.* [2010] 320 ITR 561/187 Taxman 312 (SC), the Apex Court clearly pointed out that even though the power to reopen under the amended provision post 1st April 1989 is much wider, yet, one has to give a schematic interpretation to the words "reason to believe". The Apex Court pointed out that vesting the Assessing Authority with the jurisdiction to reopen an assessment on the basis of mere change of opinion, would amount to conferring an arbitrary power on the Assessing Authority. The Apex Court reasoned out as follows:

"... We must also keep in mind the conceptual difference between power to review and power to reassess. The Assessing Officer has no power to review; he has the power to reassess. But reassessment has to be based on fulfillment of certain pre-condition and if the concept of "change of opinion" is removed, as contended on behalf of the Department, then, in the garb of reopening the assessment, review would take place. One must treat the concept of "change of opinion" as an in-built test to check abuse of power by the Assessing Officer. Hence, after 1st April, 1989, Assessing Officer has power to re-open, provided there is "tangible material" to come to the conclusion that there is escapement of income from assessment. Reasons must have a live link with the formation of the belief. Our view gets support from the changes made to section 147 of the Act, as quoted hereinabove. Under the Direct Tax Laws (Amendment) Act, 1987, Parliament not only deleted the words "reason to believe" but also inserted the word "opinion" in section 147 of the Act. However, on receipt of representations from the companies against omission of the words "reason to believe", Parliament reintroduced the said expression and deleted the word "opinion" on the ground that it would vest arbitrary powers in the Assessing Officer. We quote hereinbelow the relevant portion of Circular No. 549 dated October 31, 1989 {[1990] 182 ITR (St.) 1, 29), which reads as follows:

"7.2 Amendment made by the Amending Act, 1989, to reintroduce the expression 'reason to believe' in section 147. A number of representations were received against the omission of the words reason to believe' from section 147 and their substitution by the opinion' of the Assessing Officer. It was pointed out that the meaning of the expression, reason to believe' had been explained in a number of court rulings in the past and was well settled and its omission from section 147 would give arbitrary powers to the Assessing Officer to reopen past assessments on mere change of opinion. To allay these fears, the Amending Act, 1989, has again amended section 147 to reintroduce the expression has reason to believe' in place of the words for reasons to be recorded by him in writing, is of the opinion'. Other provisions of the new section 147, however, remain the same."

Keeping this declaration of law in the background, when we look at the original assessment made and the documents filed by the assessee, it is clear that the document on the hire purchase of the machinery entered into on 10th March 1995 and the subsequent lease agreement dated 13th of March 1995 were very much before the Assessing Authority while considering the claim of depreciation. When we look at the reassessment order dated 24.3.2000, in paragraph 4 of the order, the Assessing Authority pointed out as to the perusal of the details in the records as well as the assessee's letter dated 24.3.2000 in reply to the original assessment. As rightly pointed out by the learned counsel appearing for the assessee/respondent herein, the assessment order nowhere points out to the material which enabled the Assessing Authority to reach its conclusion that the transactions are sham and nominal or as to the material basis which enabled the Assessing Authority to reach such conclusion to reopen the assessment under Section 147. As observed by the Apex Court, a reading of the reassessment order leaves no manner of doubt that the entire exercise is a mere change of opinion and more in the nature of a review rather than a case of reassessment on discernable materials which support the assumption of jurisdiction under Section 147. In the circumstances, we agree with the Tribunal that as far the assessment year 1995-96 is concerned, the reopening of the assessment not being based on valid material but one of change of opinion, the Revenue's appeal has to be rejected on that score. Quite apart from this aspect, we have no hesitation in rejecting the Revenue's appeal on the merits of the reassessment relating to the assessment year 1995-96 as well as in respect of the assessment years 1996-97 and 1997-98.

9. We have already narrated the facts in the preceding paragraphs as regards the transactions involved herein. The assessee had purchased the machinery on 10.03.1995 from M/s. Ponni Sugars and Chemicals Limited, a sister concern of the assessee herein at a cost of Rs.250 lakhs. It is no doubt true that the machinery were embedded and were in possession of the seller M/s. Ponni Sugars and Chemicals Limited at the time of sale. The assessee took constructive delivery of the machinery which were there with M/s. Ponni Sugars and Chemicals Ltd. One of the grounds taken by the Assessing Authority in respect of all these assessment years for rejecting the claim of the assessee was that it was never in possession of the machinery. Given the fact that law recognises constructive delivery as an acceptable mode of delivery and possession, the fact that the assessee had not taken physical possession, per se, does not pronounce anything against the sale that took place between the assessee and M/s. Ponni Sugars and Chemicals Limited. Thus there are no material on record to show that the sale between the assessee and M/s. Ponni Sugars and Chemicals Limited was a sham transaction. In the above circumstances, the genuineness of the said transaction cannot be questioned at all.

10. The second aspect of the transaction is the hire purchase agreement between the assessee and Wipro Finance Limited. As already pointed out, the total consideration of the purchase of the material was Rs.250 lakhs, for which the assessee had paid a sum of Rs.50 lakhs and the balance of Rs. 200 lakhs was financed by M/s. Wipro Finance Limited. As far as this transaction is concerned, a perusal of the same shows that the records were

available before the Assessing Authority at the earliest of the transactions which related to the assessment year 1995-96 and there is nothing on record to show that the transaction had not gone through between the assessee and M/s. Wipro Finance Limited. The only ground on which the Revenue seeks to question this agreement is the minutes of the meeting of the Board of Directors of M/s. Ponni Sugars and Chemicals Limited where there is a reference to the sale of the machinery to meet the financial needs of the said company. The monthly payment by the assessee to M/s. Wipro Finance Limited was to be met by the rental dues payable by M/s. Ponni Sugars and Chemicals Ltd. to M/s. Wipro Finance Limited, being made to meet the monthly payment of the assessee company to M/s. Wipro Finance Limited. The Revenue laid stress on this aspect of M/s. Ponni Sugars and Chemicals Limited making payment to M/s. Wipro Finance Limited of the rental dues as by way of satisfaction of the assessee's commitments under the hire purchase agreement. As far as this aspect is concerned, when we look at the agreement between the assessee and M/s. Wipro Finance Limited and between the assessee and M/s. Ponni Sugars and Chemicals Limited, we do not find any material by which one may say that the lessee M/s. Ponni Sugars and Chemicals Limited had undertaken under the said agreement the responsibility of meeting the liabilities of the assessee company to M/s. Wipro Finance Limited. In fact, in Article 4, under Clause 4.1.1, the lessee company had undertaken to pay the lease rentals on the due date as specified under the First Schedule and that the last payment was to be made by the assessee herein. A copy of the instalments paid by the assessee to M/s. Wipro Finance Limited for the assessment year 1996-97 also figures in as one of the documents filed before this Court. Leaving this aspect aside, even assuming that the lessee company had undertaken such responsibility to meet the liability of the assessee company to pay the hire purchase amount to M/s. Wipro Finance Limited, we fail to understand how this circumstance would, in any manner, lead to the inference that the agreement is a sham one, for, it is a matter of pure commercial understanding between two parties under the agreement to decide as to the modalities of lease rental payment. In the light of the above, we do not find any material other than what had been mentioned above and considered by the Officer at the original assessment as placed by the assessee, to come to a definite conclusion on the character of the transaction as had been alleged by the Revenue. Given the freedom to enter into agreements with parties and guided by commercial considerations, even to invoke the theory of tax evasion, the Revenue must have sufficient material to draw an inference of what had been shown as an understanding on an agreement between the parties, is not, in fact, so.

11. In the recent decision of the Apex Court in *Vodafone International Holdings B.V*. v. *Union of India* [2012] 341 ITR 1/204 Taxman 408/17 taxmann.com 202 (SC), the Apex Court considered the decision in *McDowell & Co. Ltd.* (*supra*) extensively and held that there is no conflict between the decision in *McDowell & Co. Ltd.'s* case (*supra*) and *Union of India* v. *Azadi Bachao Andolan* [2003] 132 Taxman 373 (SC) or *McDowell & Co. Ltd.* (*supra*) and *Mathuram Agarwal* v. *State of Madhya Pradesh* [1999] 8 SCC 667. The Apex Court pointed out that the task of the Revenue/Court is to ascertain the legal nature of the transaction and while doing so, it has to look at the entire transaction as a whole and not to adopt a dissecting approach. The Apex Court pointed out that "the Revenue cannot start with the question as to whether the impugned transaction is a tax deferment/saving device but that it should apply the "look at" test to ascertain its true legal nature [See *Craven* v. *White* (*supra*)] which further observed that genuine strategic tax planning has not been abandoned by any decision of the English courts till date."

12. Thus, affirming the view taken in *McDowell & Co. Ltd.'s* case (*supra*), the Apex Court pointed out that colourable devices cannot be a part of tax planning. The Apex Court pointed out that it cannot be said that all tax planning is illegal/illegitimate/impermissible. Applying the rationale of this decision to the case on hand, in the absence of any material to pronounce on the genuineness of the transaction herein, the mere fact that what had been

purchased had been leased out to the vendor or that vendor had undertaken to pay the hire charges on behalf of the assessee to the hire purchase company, per se, cannot lead to a conclusion that the transaction is a sham one. In the circumstances, even invoking the decision in McDowell case, we do not find any ground to accept the plea of the Revenue that the claim of the assessee has to be rejected as a sham one.

13. Incidentally, it may also be pointed out that in respect of the assessment year 1998-99, the assessee claimed capital gains on the sale of the machinery. Even though the said claim was rejected, on appeal, by order dated 13.12.2002, the Commissioner of Income Tax (Appeals) allowed the claim by applying the decision of the Income Tax Appellate Tribunal, relating to the assessment years 1995-96 to 1997-98. Evidently, the Revenue had not gone on appeal as against the order of the Commissioner of Income Tax (Appeals). Whatever be correctness or otherwise of the claim of the Revenue, it is a matter of relevance herein to point out that in respect of the assessment year 1998-99, the Commissioner of Income Tax invoked his jurisdiction under Section 263 by issuing notice on 28.1.2003. Further, on 10.2.2003, the said proceeding was dropped by the Commissioner of Income Tax (Appeals).

14. The above facts are referred only to point out to the mind of the Department in the matter of granting the relief to the assessee on the transactions, that while for one year it had accepted the transactions as a genuine one, viz., 1998-99, in respect of assessment years 1995-96 to 1997-98, it took a different stand that it is a colourable transaction. On a perusal of the documents produced, we have no hesitation in confirming the order of the Tribunal, both on the question of jurisdiction to reopen the assessment for the assessment year 1995-96 and on the merits of the claim in respect of the three assessment years viz., 1995-96 to 1997-98.

In the result, all these Tax Case Appeals stand dismissed. No costs.