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IN THE HIGH COURT OF DELHI AT NEW DELHI

Date of decision: 18th December, 2013

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W.P.(C) 1992/2013

M/S ORTEL COMMUNICATIONS LTD Petitioner
Through Mr. Yogesh Jagia and Mr. Amit Sood
Advocates.

versus

DY. COMMISSIONER OF INCOME TAX Respondent
Through Ms. Suruchi Aggarwal, Sr. Standing
Counsel.

CORAM:

HON'BLE MR. JUSTICE SANJIV KHANNA

HON'BLE MR. JUSTICE SANJEEV SACHDEVA

SANJIV KHANNA, J. (ORAL)

Ortel Communications Limited by this writ petition impugns reassessment notice dated 26th March, 2012 issued under Section 147 read with Section 148 of the Income Tax Act, 1961 (Act, for short). The petitioner has also impugned order dated 14th February, 2013 by which objections to the reassessment notice have been rejected.

2. The petitioner is a company and for assessment year 2007-08 had filed their return of income on 29th October, 2007 declaring 'NIL' income. The case was taken up for scrutiny assessment and assessment order dated 24th December, 2009 was passed in which disallowances/additions were made on account of fixed assets written

Signature Not Verified off of Rs.44,68,170/- and sundry creditors outstanding since 31st

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been compared and the digital data is as per
the physical file and no page is missing.

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March, 2003 of Rs.3,70,231/-. However, income of the assessee was determined at 'NIL' after giving set off ^{to} brought forward losses and book profits were determined at Rs.2,01,39,407/- under Section 115JB of the Act. We shall refer to the original assessment proceedings and the communications addressed by the petitioner-assessee in the said proceedings, subsequently.

3. After the original assessment, audit objection was raised that the petitioner had claimed and was allowed expenditure of Rs.3,22,93,098/- on account of bandwidth cost in the profit and loss account. The audit objection records that the amount had been paid to upgrade the bandwidth and the expenditure incurred gave enduring benefit and, therefore, was required to be capitalised and added back to the income of the petitioner.

4. Thereafter, the Assessing Officer recorded the following 'reasons to believe' and issued notice under Section 147 read with Section 148 of the Act:-

"The perusal of the assessment records of M/s Ortel Communications for the assessment year 2007-08 revealed that the assessee claimed and was allowed expenditure of Rs.3,22,93,098/- on account of bandwidth cost in the profit and loss account. The same has been paid to upgrade its Bandwidth. Since, this expenditure gave an enduring benefit: of the assessee, it was required to be capitalized and added back to the income of the assessee. The mistake resulted in under assessment of income of Rs.3,22,93,098/- involving tax effect of

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Rs.1,08,69,855/-.”

5. The contention of the petitioner is that the ‘reasons to believe’ recorded above are factually incorrect and even otherwise a mere surmise and conjecture. This was a case of ‘change of opinion’ as this aspect and question was specifically answered and adverted to in the original assessment proceedings. Learned counsel for the respondents, on the other hand, submits that the Assessing Officer had not examined and considered the question whether the bandwidth upgradation cost was capital or revenue expenditure and, therefore, it is a case of ‘non-application or non-consideration’ and not ‘change of opinion’.

6. The petitioner-assessee was engaged in the business of building and operating Hybrid Fibre Coaxial (HFC) broadband communications networks in the State of Orissa. They provide cable TV, high speed internet services and telephone services. The cable network was designed and constructed with return path capability and was capable of providing high-speed cable modem service.

7. In the written submission filed before the Assessing Officer during the course of original assessment proceedings with reference to bandwidth cost of Rs.3,22,93,098/-, the petitioner-assessee had specifically stated as under:-

“That during the year under assessment, company
Incurred bandwidth cost of Rs 3,22,93,098/- to

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enhance the capacity to transfer the data which is necessary to match with upgrading technology. Amount was paid to Reliance communications, Railtel and VSNL. Bandwidth was upgraded from E3 level to DS 3 level. Expenses incurred has been claimed in profit and loss account being revenue exp. [Copies of Assessment Order, order passed by CIT (A) and Hon'ble ITAT, Delhi for AY 2001-02 and 2002-03 along with copies of Assessment order and order of CIT (A) for AY 2003-04, 2004-05 and 2005-06 with copy of assessment order of AY 2006-07 are annexed and marked as **Annexure —1.**][colly].”

8. In the profit and loss account under the head ‘expenditure’ bandwidth cost of Rs.3,22,93,098/- has been separately and specifically declared and claimed as a revenue expense. It is evident from the reply quoted above that the petitioner on being questioned about the said expenditure, had highlighted the nature and character of the expenditure to the Assessing Officer and had enclosed copy of the earlier assessment orders etc. It was stated that bandwidth was upgraded from E3 level to DS3 level and the amount was paid to Reliance Communications, Railtel and VSNL for the said purpose. The said expenditure was claimed as revenue expenditure in the profit and loss account. The said statement was made in clear and categorical term without any ambiguity or doubt. It was not a fact or an entry which required elucidation i.e. an entry which was hidden or had to be deciphered. The claim of the petitioner was raised and stated.

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9. In view of the aforesaid position, the submission of the Revenue that during the original assessment proceedings, expenditure incurred to upgrade bandwidth from E3 level to DS3 level which was not revenue but capital had escaped notice and thus not examined, is not acceptable. The letter/written submissions filed by the petitioner quoted above, clearly indicates that the Assessing Officer had raised a query and answer to the same was furnished by the assessee. It may not be possible to ascertain, how and in what manner query was raised, but the undisputed position and accepted factual position is that the aforesaid response was filed before the Assessing Officer. It is obvious that the said response had a precursor and antecedent. The petitioner had given details and particulars of the said expense.

10. It transpires that after audit objection was raised, the petitioner was asked to respondents and had submitted a letter dated 20th September, 2010 to the Assessing Officer. In the said letter it was reiterated:-

“Since the bandwidth refers to the capacity of the cables to transmit the data therefore, no question arise about acquiring such cables by the assessee company because the assessee company has been availing bandwidth from M/s Reliance Communications Ltd, Railtel & VSNL to provide internet services to all its subscribers as is the case with other internet service providers like MTNL, BSNL, Airtel etc who have been availing bandwidth from other service providers. The company pays the

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bandwidth cost to the company who is providing bandwidth for to transmit the data on the internet and the cost is payable according to the capacity of the bandwidth availed. During the year the company has upgraded its bandwidth purchases to E3 level and DS3 level so to provide improved services to its subscriber which reduce the cost of the company as well as of the subscriber because with this upgradation services the subscriber is able to transmit the data or download the data at a higher speed with a lesser time. The company has not incurred any capital expenditure for upgrading its bandwidth because technological developments caused these changes on regular basis as is the normal case with other services like mobile telephone which were originally confined to only mobile telephone services whereas today with the technological development value added services like e-mails, video and audio download are also being provided. Since the company has not incurred any expenditure for making out a new asset and the amount claimed was paid only for availing the transmission of its data therefore, the same is allowable as revenue expense."

11. Thus, the aforesaid explanation of the petitioner-assessee was available before the Assessing Officer and was on record before 'reasons to believe' were recorded on 26th March, 2012.

12. The Assessing Officer in response to the audit query and before recording reasons to believe had accepted the said factual position and had accordingly replied that the audit objection was not acceptable.

The Assessing Officer had elucidate:-

"A letter was issued to the assessee asking for a written reply on the above said audit objection. The assessee has submitted a written reply (copy enclosed) on 20.09.2010 intimating that during the year the assessee upgraded its bandwidth purchased to E3 level

and DS3 level so to provide improved services to its subscriber which reduce the cost of the company as well as of the subscriber because with this upgradation services the subscriber is able to transmit the data or download the data at a higher speed with a lesser time. The company has not incurred any capital expenditure for making out a new asset. The amount claimed was paid for availing the transmission of its data. Further, the assessee has claimed the similar expenditure in earlier years also."

(emphasis supplied)

13. Similar submission was made in the objections raised by the petitioner before the Assessing Officer to the reassessment notice. It was specifically pleaded:-

3. That the assessee company in the normal course of business has been claiming bandwidth cost as revenue exp since assessment year 2001-2002 and the detail of bandwidth cost claimed and allowed in the assessments completed under section 143(3) of Act is as under: -

Assessment year	Bandwidth claimed cost	Detail of assessment order
2001-2002	16,98,380	143(3)
2002-2003	22,65,098	143(3)
2003-2004	27,72,433	143(3)
2004-2005	64,34,524	143(3)
2005-2006	1,17,44,587	143(3)
2006-2007	2,53,94,261	143(3)
2007-2008	3,22,93,098	143(3)

4. That in the assessment year 2007-2008 assessee

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company claimed band width cost of Rs. 3,22,93,098/- and in para 5.2 of the 12th annual report it was mentioned that the company has upgraded its bandwidth purchase to E3 and DS3 level in the current year. The relevant paragraphs inter-alia reads: -

"Your company is well equipped with its upgraded Network Operating Centre (NOC) with inability redundancy of key elements in the system to support and sustain the higher level of customer base and service. The company is planning substantial investment in key network equipments such as fiberization and node powering which will increase the uptime of the services. The company has upgraded its purchases to E3 and DS3 level in the current year. This apart from bringing in substantial cause reduction of bandwidth charges, will improve the customer experience of high speed internet."

5. That the assessee during the assessment year made payment of bandwidth cost to the followings: -

a) Reliance Communications Ltd.	Rs. 3,11,38,210/-
b) Railtel	Rs. 4,32,879/-
c) VSNL	Rs. 7,22,012/-

6. Assessee submits that the bandwidth is only the capacity to transfer data through cable on internet and upgrading the bandwidth refer to increasing its capacity to transmit the data which does not create any new asset. Increasing bandwidth is akin to wheeling of electricity on the network installed by the distribution companies. The meaning of the bandwidth is available on net in www.wikipedia.org is annexed and marked as Annexure-3."

14. It was further submitted in the objections:-

"Assessee submits that admittedly the notice under section 148 has been issued based on the material that was already available on record even at the time of completing assessment under section 143(3) of Act and further notice has been issued merely based upon the audit objections raised by the audit party by acting as post office simplicitor and without satisfying the sine-qua-non of section 147 of Act and hence the notice issued is liable to be withdrawn."

15. In the impugned order dated 14th February, 2013, the Assessing Officer while rejecting the objections has not dealt with the aforesaid submission and contention. The impugned order refers to the case law but not the factual matrix and the issue in question. This is not the correct way to deal with objections in which factual aspects have been raised and it has been submitted that the issue was considered and debated in the first round and 'reasons to believe' as recorded were surmises and conjectures and did not have any foundation or basis. The contention of the petitioner, therefore, has not been dealt with in the order disposing of the objections. Even in the counter affidavit filed by the respondents, there is no averment negating and contradicting the factual matrix.

16. The petitioner, it is accepted, was providing broadband services. To provide improved and better services to their subscribers, they had upgraded bandwidth from E3 level to DS3 level. The amount was paid to third parties from whom the petitioner had procured bandwidth services. It is not the case where the petitioner had upgraded their assets to provide superior bandwidth from E3 level to DS3 level. No expenditure was incurred on upgrading or towards fixed assets/capital owned by the petitioner. This is neither averred nor stated in the 'reasons to believe' or even in the order rejecting objections to reopening. The note prepared by the Assessing Officer in

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response to the audit objection is to the contrary and states that the assessee had not upgraded or enhanced the bandwidth capacity of his own fixed assets. There is no allegation or assertion that the allegation is false or wrong. That apart, we have already noted that the question whether the expenditure incurred on upgradation of bandwidth was revenue or capital in nature was specifically adverted to and answered by the petitioner-assessee during the course of original assessment proceedings. The Assessing Officer accepted the stand and did not make any addition.

17. In the aforesaid factual position, ratio of the Full Bench's decision in *Commissioner of Income Tax Vs. Usha International Ltd.* [2012] 348 ITR 485 (Delhi) is applicable on two counts; (i) 'change of opinion' and (ii) 'reasons to believe' do not show any nexus and prima facie show and indicate that income chargeable to tax had escaped assessment. We would like to reproduce the following paragraphs from the judgment in the case of *Usha International Ltd.* (supra):-

"12. The said observations have been rightly held to be contrary to the Full Bench decision of the Delhi High Court in *Kelvinator of India Ltd.* [2002] 256 ITR 1 (Delhi) [FB] in *Eicher Ltd.* [2007] 294 ITR 310 (Delhi). The said decision in *Eicher Ltd.* (supra) makes reference to the decision of *KLM Royal Dutch Airlines v. Asst. Director of I. T.* [2007] 292 ITR 49 (Delhi). *KLM Royal* case (supra) deals with some other issues on which we do not express or make any observation approving or disapproving. Some of these aspects have been considered and explained in other decisions in the light of the judgment of the Supreme Court in the case of *Rajesh Jhaveri Stock Brokers Pvt. Ltd.*

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[2007] 291 ITR 500 (SC).

13. It is, therefore, clear from the aforesaid position that :

(1) Reassessment proceedings can be validly initiated in case return of income is processed under section 143(1) and no scrutiny assessment is undertaken. In such cases there is no change of opinion.

(2) Reassessment proceedings will be invalid in case the assessment order itself records that the issue was raised and is decided in favour of the assessee. Reassessment proceedings in the said cases will be hit by the principle of "change of opinion".

(3) Reassessment proceedings will be invalid in case an issue or query is raised and answered by the assessee in original assessment proceedings but thereafter the Assessing Officer does not make any addition in the assessment order. In such situations it should be accepted that the issue was examined but the Assessing Officer did not find any ground or reason to make addition or reject the stand of the assessee. He forms an opinion.

The reassessment will be invalid because the Assessing Officer had formed an opinion in the original assessment, though he had not recorded his reasons.

14. In the second and third situation, the Revenue is not without remedy. In case the assessment order is erroneous and prejudicial to the interest of the Revenue, they are entitled to and can invoke power under section 263 of the Act. This aspect and position has been highlighted in CIT v. DLF Power Ltd. I. T. A. No. 973 of 2011 decided on November 29, 2011-since reported in [2012] 345 ITR 446 (Delhi) and BLB Ltd. v. Asst. CIT Writ Petition (Civil) No. 6884 of 2010 decided on December 1, 2011-since reported in [2012] 343 ITR 129 (Delhi). In the last decision it has been observed (page 135) :

"The Revenue had the option, but did not take recourse to section 263 of the Act, in spite of audit objection. Supervisory and revisionary power under section 263 of the Act is available, if an order passed by the Assessing Officer is erroneous and prejudicial to the interest of the Revenue.

An erroneous order contrary to law that has caused prejudiced can be correct, when jurisdiction under section 263 is invoked."

15. Thus, where an Assessing Officer incorrectly or erroneously applies law or comes to a wrong conclusion and income chargeable to tax has escaped assessment, resort to section 263 of the Act is available and should be resorted to. But initiation of reassessment proceedings will be invalid on the ground of change of opinion.

16. Here we must draw a distinction between erroneous application/inter-pretation/understanding of law and cases where fresh or new factual information comes to the knowledge of the Assessing Officer subsequent to the passing of the assessment order. If new facts, material or information comes to the knowledge of the Assessing Officer, which was not on record and available at the time of the assessment order, the principle of "change of opinion" will not apply. The reason is that "opinion" is formed on facts. "Opinion" formed or based on wrong and incorrect facts or which are belied and untrue do not get protection and cover under the principle of "change of opinion". Factual information or material which was incorrect or was not available with the Assessing Officer at the time of original assessment would justify initiation of reassessment proceedings. The requirement in such cases is that the information or material available should relate to material facts. The expression "material facts" means those facts which if taken into account would have an adverse effect on the assessee by a higher assessment of income than the one actually made. They should be proximate and not have remote bearing on the assessment. The omission to disclose may be deliberate or inadvertent. The question of concealment is not relevant and is not a precondition which confers jurisdiction to reopen the assessment.

17..... The aforesaid decisions/facts cases must be distinguished from cases where the material facts on record are correct but the Assessing Officer did not draw proper legal inference or did not appreciate the implications or did not apply the correct law. The second category will be a case of "change of opinion" and cannot be reopened for the reason that the

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assessee, as required, has placed on record primary factual material but on the basis of legal understanding, the Assessing Officer has taken a particular legal view. However, as stated above, an erroneous decision, which is also prejudicial to the interests of the Revenue, can be made subject-matter of adjudication under section 263 of the Act."

18. In *Usha International* (supra) reference was made to the decision of the Supreme Court in *CIT Vs. P. V. S. Beedies P. Ltd.* [1999] 237 ITR 13 (SC) and the following passage from the judgment in the case of *New Light Trading Co. v. Commissioner of Income-tax* [2002] 256 ITR 0391 (Del) was quoted:-

"In the case of CIT v. P. V. S. Beedies P. Ltd. [1999] 237 ITR 13 (SC), the apex court held that the audit party can point out a fact, which has been overlooked by the Income-tax Officer in the assessment. Though there cannot be any interpretation of law by the audit party, it is entitled to point out a factual error or omission in the assessment and reopening of a case on the basis of factual error or omission pointed out by the audit party is permissible under law. As the Tribunal has rightly noticed, this was not a case of the Assessing Officer merely acting at the behest of the audit party or on its report. It has independently examined the materials collected by the audit party in its report and has come to an independent conclusion that there was escapement of income. The answer to the question is, therefore, in the affirmative, in favour of the Revenue and against the assessee."

19. The present case clearly is not a case where entry or claim/deduction was not examined by the Assessing Officer. It was

examined and even answered by the petitioner. No factual error or omission is pointed out or referred.

20. On the second aspect we would like to quote the following paragraph from *Usha International* (supra):-

“As recorded above, the reasons recorded or the documents available must show nexus that in fact they are germane and relevant to the subjective opinion formed by the Assessing Officer regarding escapement of income. At the same time, it is not the requirement that the Assessing Officer should have finally ascertained escapement of income by recording conclusive findings. The final ascertainment takes place when the final or reassessment order is passed. It is enough if the Assessing Officer can show tentatively or prima facie on the basis of the reasons recorded and with reference to the documents available on record that income has escaped assessment.”

21. It would be appropriate to refer to the decision of the Supreme Court in *Sheo Nath Singh v. ACIT*, (1971) 82 ITR 147 wherein interpreting the expression “reason to believe”, it was held:

“ There can be no manner of doubt that the words ‘reason to believe’ suggest that the belief must be that of an honest and reasonable person based upon reasonable grounds and that the Income-tax Officer may act on direct or circumstantial evidence but not on mere suspicion, gossip or rumour. The Income-tax Officer would be acting without jurisdiction if the reason for his belief that the conditions are satisfied does not exist or is not material or relevant to the belief required by the section. The court can always examine this aspect though the declaration or sufficiency of the reasons for the belief cannot be investigated by the court.” (Emphasis supplied)

22. In **Ganga Saran & Sons (P) Ltd. v. ITO**, (1981)130 ITR 1 (SC), it has been observed as under:

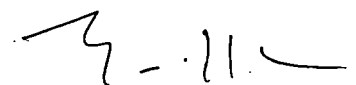
“ The important words under s. 147(a) are “has reason to believe” and these words are stronger than the words “is satisfied”. *The belief entertained by the ITO must not be arbitrary or irrational. It must be reasonable or , in other words, it must be based on reasons which are relevant and material.* The court, of course, cannot investigate into the adequacy or sufficiency of the reasons which have weighed with the ITO in coming to the belief, but the court can certainly examine whether the reasons are relevant and have a bearing on the matters in regard to which he is required to entertain the belief before he can issue notice under S.147(a). *if there is no rational and intelligible nexus between the reasons and the belief, so that, on such reasons, no one properly instructed on facts and law could reasonably entertain the belief, the conclusion would be inescapable that the ITO could not have reason to believe that any part of the income of the assessee had escaped assessment* and such escapement was by reason of the omission or failure on the part of the assessee to disclose fully and truly all material facts and the notice issued by him would be liable to be struck down as invalid.”

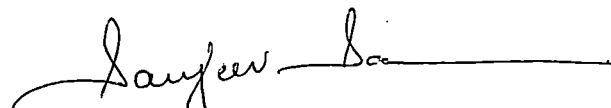
23. Referring to the said judgment in the case of **ACIT v. Rajesh Jhaveri Stock Brokers (P) Ltd.** (2007) 291 ITR 500 (SC), it was elucidated:-

“16. Section 147 authorises and permits the Assessing Officer to assess or reassess income chargeable to tax if he has reason to believe that income for any assessment year has escaped assessment. The word “reason” in the phrase “reason to believe” would mean cause or justification. If the Assessing Officer has cause or justification to know or suppose that income had escaped assessment, it can be said to have reason to believe that an income had escaped assessment. The expression cannot be read to mean that the Assessing Officer should have finally ascertained the fact by legal

evidence or conclusion. The function of the Assessing Officer is to administer the statute with solicitude for the public exchequer with an inbuilt idea of fairness to taxpayers. As observed by the Delhi High Court in *Central Provinces Manganese Ore Co. Ltd. v. ITO* [1991 (191) ITR 662], for initiation of action under section 147(a) (as the provision stood at the relevant time) fulfillment of the two requisite conditions in that regard is essential. At that stage, the final outcome of the proceeding is not relevant. In other words, at the initiation stage, what is required is "reason to believe", but not the established fact of escapement of income. At the stage of issue of notice, the only question is whether there was relevant material on which a reasonable person could have formed a requisite belief. Whether the materials would conclusively prove the escapement is not the concern at that stage. This is so because the formation of belief by the Assessing Officer is within the realm of subjective satisfaction (see *ITO v. Selected Dalurband Coal Co. Pvt. Ltd.* [1996 (217) ITR 597 (SC)]; *Raymond Woollen Mills Ltd. v. ITO* [1999 (236) ITR 34 (SC)]."

24. In view of the aforesaid position, the writ petition is allowed and the reassessment notice and proceedings are quashed/set aside. No costs.


SANJIV KHANNA, J


SANJEEV SACHDEVA, J

DECEMBER 18, 2013
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