In the High Court of Judicature at Madras

Dated: 4.12.2007

Coram:

The Honourable Mr.Justice K.Raviraja Pandian
and
The Honourable Mrs.Justice Chitra Venkataraman

Tax Case (Appeal) No.1464 of 2007

The Commissioner of Income Tax,
Tamil Nadu-I, Madras. .. Appellant

vs.

M/s.Kamy Software Solutions (P) Ltd.,
M5F, MIG Flats, Latice Bridge Road,
Thiruvanmiyur, Chennai-600 041. .. Respondent

Tax Case (Appeal) against the order of the Income Tax Appellate Tribunal "B" Bench, Chennai, dated 16.2.2007 in I.T.A.No.1235/Mds/2002 & 101/Mds/2006 against the order of the Commissioner of Income Tax (Appeals)V, Chennai for the year of 1997-98 dated 5.6.2000 in ITA.NO.195/99-2000 and the order of the Commissioner of Income Tax (Appeals)XI, Chennai dated 30.5.2002 in ITA.NO.328/2001-02 against the order of the Deputy Commissioner of Income Tax Company circle I(3) Chennai-34 for the year of 1997-98 dated 7.1.2000 in PA NO.GIR.NO.170K.

For appellant : Mr.J.Naresh Kumar

Judgment

(The Judgment of the Court was delivered by K.Raviraja Pandian,J)

The appeal is against the order of the Tribunal in I.T.A.No..1235/Mds/2002 & 101/Mds/2006. The relevant assessment year is 1997-1998.

2. The assessee (respondent-Company) is dealing in software export technical services related to software. The assessee claimed deduction under Section 80-HHE of the Income Tax Act (hereinafter referred to as 'the Act') in connection with the services rendered for the development of software abroad. During the course of assessment proceedings, in order to verify the claim of the assessee in regard to deduction under Section 80-HHE of the Act, a survey under Section 133-A of the Act was carried out in the

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business premises of the assessee on 29.9.1998. During the course of survey operations, the assessing officer found several agreement in regard to job placement and obtained copies of the documents.

3. The assessing officer, on the basis of the agreement, came to the conclusion that the assessee was not engaged in the business of providing technical services outside India in connection with the development or production of computer software, but was only a human resource services and in that view of the matter, the assesssing officer held that the assessee was not entitled for the benefit of deduction under Section 80-HHE of the Income Tax Act and disallowed the claim of the assessee.

4. The Commissioner of Income Tax (Appeals) confirmed the action of the assessing officer. That order has become final, as the assessee has not agitated the matter any further.

5. After the decision of the quantum appeal, the assessing officer initiated penalty proceedings under Section 271(1)(c) of the Act on 19.1.2000 and imposed penalty. Against that order, the assessee preferred appeal before the Commissioner of Income Tax, who has confirmed the order of the assessing officer. The correctness of the said order was carried on by way of further appeal to the Income Tax Appellate Tribunal by the assessee. The Tribunal held in favour of the assessee on the ground that there is no need to impose any penalty, as the assessee has never filed inaccurate particulars nor concealed the income and on that basis, the Tribunal allowed the appeal. Challenging the correctness of the same, this appeal is before us by formulating the following question of law:

> "Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was right in law in deleting the penalty under Section 271(1)(c) of the Act, is valid in law?"

6. We have heard the learned Standing Counsel appearing on behalf of the appellant-Revenue and perused the materials including the impugned order of the Tribunal.

7. Before the Tribunal, learned counsel for the assessee has filed a copy of the Notification in No.11521, dated 26.9.2000 and argued that the Central Board of Direct Taxes allowed the deduction under Section 80-HHE or under Section 10-A of the Act in regard to human resource services as mentioned in sub-clause (vii) of the Notification and subsequently, vide Circular No.3 of 2004, dated 12.2.2004, the Board has clarified the position in favour of the assessee. The Tribunal has also extracted the Board's Circular, which reads as follows:

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"Circular No.3 of 2004, dt.12th Feb. 2004

Sub: Clarification regarding provisions of section 80HHE of the Income-tax Act, 1961

The Board has received references seeking clarification on the period of applicability of the Explanation under Section 80HHE(1) of the Income-tax Act, 1961. The Explanation states as under--

> "For the removal of doubts, it is hereby declared that the profits and gains derived from on site development of computer software (including services for development of software) outside India shall be deemed to be the profits and gains derived from the export of computer software outside India."

1.1. The Explanation was inserted by the Finance Act, 2001 with effect from 1st April, 2001. However, as pointed out by the Ministry of Law on various occasions, the use of the words "for the removal of doubts" in an Explanation normally implies that the Explanation is only clarificatory in nature. As this Explanation under Section 80-HHE (1) only clarifies the existing position of law, the Board are of the opinion that the Explanation will be considered to have effect from 1st April, 1991, i.e the date on which section 80-HHE came into force.

2. The contents of this Circular may be given wide publicity."

8. In view of Circular No.3 of 2004, dated 12.2.2004 and on the facts of the case, the Tribunal has come to the conclusion that the assessee was under the bona-fide belief that the services rendered by the assessee-Company constitute technical services and the assessee was entitled to deduction under Section 80-HHE of the Act. The Tribunal further recorded a clear and categoric finding to the effect that the assessee never filed inaccurate particulars nor concealed particulars of income so as to come within the mischief of Section 271(1)(c) of the Income Tax Act.

9. The very same provision, namely Section 80-HHE of the Act came to be considered by the Supreme Court in the decision reported

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in [{2007} 292 ITR 11 (SC)] (T.Ashok Pai vs. CIT). The Supreme Court in that decision held as follows:

> "It is therefore, trite that if an explanation given by the assessee with regard to the mistake committed by him has been treated to be bona fide and it has been found as of fact that he had acted on the basis of wrong legal advice, the question of his failure to discharge his burden in terms of the Explanation appended to section 271(1)(c) of the Income-tax Act would not arise.
>
> In Dilip N. Shroff v. Joint CIT (Civil appeal arising out of SLP (C) No.26831/2004) delivered today (2007) 291 ITR 519 (SC), this Court observed (see page 546 of 291 ITR):
>
> "The expression 'conceal' is of great importance. According to Law Lexicon, the word 'conceal' means:
>
> 'to hide or keep secret. The word 'conceal' is con+celare which implies to hide. It means to hide or withdraw from observation; to cover or keep from sight; to prevent the discovery of; to withhold knowledge of. The offence of concealment is, thus, a direct attempt to hide an item of income or a portion thereof from the knowledge of the income-tax authorities.'
>
> In Webster's Dictionary, 'inaccurate' has been defined as:
>
> 'not accurate', not exact or correct; not according to truth;; erroneous; as an inaccurate statement, copy or transcript."
>
> It signifies a deliberate act or omission on the part of the assessee. Such deliberate act must be either for the purpose of concealment of income or furnishing of inaccurate particulars.
>
> The term "inaccurate particulars" is not defined. Furnishing of an assessment of value of the property may not by itself be furnishing of inaccurate particulars. Even if the explanations are taken recourse to, a finding has to be arrived at having regard to clause (A) of Explanation 1 that the Assessing Officer is required to arrive at a finding that the explanation offered by an assessee, in the event he offers one was false. He must be found to have failed to prove that such explanation is not only not bona fide but all the facts

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relating to the same and material to the income were not disclosed by him. Thus, apart from his explanation being not bona fide, it should have been found as of fact that he has not disclosed all the facts which were material to the computation of his income.

The explanation having regard to the decisions of this court, must be preceded by a finding as to how and in what manner he furnished the particulars of his income. It is beyond any doubt or dispute that for the said purpose the Income-tax Officer must arrive at his satisfaction in this behalf. (See CIT v. Ram Commercial Enterprises Ltd. [2000] 246 ITR 568 (Delhi) and Diwan Enterprises v. CIT [2000] 246 ITR 571 (Delhi)).

The order imposing penalty is quasi-criminal in nature and, thus, the burden lies on the Department to establish that the assessee had concealed his income. Since the burden of proof in penalty proceedings varies from that in the assessment proceeding, a finding in an assessment proceeding that a particular receipt is income cannot automatically be adopted, though a finding in the assessment proceeding constitutes good evidence in the penalty proceeding. In the penalty proceedings, thus, the authorities must consider the matter afresh as the question has to be considered from a different angle.

It is now a well-settled principle of law that the more stringent the law, the more strict a construction thereof would be necessary. Even when the burden is required to be discharged by an assessee, it would not be as heavy as the prosecution. (See P.N.Krishna Lal v. Government of Kerala [1995] Supp 2 SCC 187).

The omission of the word "deliberate", thus, may not be of much significance.

Section 271(1)(c) remains a penal statute. The rule of strict construction shall apply thereto. The ingredients for imposing penalty remain the same. The purpose of the Legislature that it is meant to be a deterrent to tax evasion is evidenced by the increase in the quantum of penalty, from 20 per cent. under the 1922 Act to 300 per cent in 1985.

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"Concealment of income" and "furnishing of inaccurate particulars" carry different connotations. Concealment refers to a deliberate act on the part of the assessee. A mere omission or negligence would not constitute a deliberate act of suppressio veri or suggestio falsi.

We may notice that in Addl. CIT v. Jeevan Lal Sah [1994] 205 ITR 244 this Court dealt with the amendment of section 271(1)(c) made in the year 1964 to hold (page 248):

> "Even after the amendment of 1964, the penalty proceedings, it is evident, continue to be penal proceedings. Similarly, the question whether the assessee has concealed the particulars of his income or has furnished inaccurate particulars of his income continues to remain a question of fact. Whether the Explanation has made a difference is — while deciding the said question of fact the presumption created by it has to be applied, which has the effect of shifting the burden of proof. The entire material on record has to be considered keeping in mind the said presumption and a finding recorded."

The question came for consideration of this court yet again in K.C.Builders v. Asst. CIT [2004] 265 ITR 562; [2004] 2 SCC 731 wherein it was held (page 569):

> "One of the amendments made to the abovementioned provisions is the omission of the word 'deliberately' from the expression 'deliberately furnished inaccurate particulars of such income'. It is implicit in the word 'concealed' that there has been a deliberate act on the part of the assessee. The meaning of the word 'concealment' as found in Shorter Oxford English Dictionary, third edition, Volume I, is as follows:
>
> 'In law, the intentional suppression of truth or fact known, to the injury or prejudice of another.'
>
> The word 'concealment' inherently carried with it the element of mens rea. Therefore, the mere fact that some figure

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or some particulars have been disclosed by itself, even if it takes out the case from the purview of non-disclosure, it cannot by itself take out the case from the purview of furnishing inaccurate particulars. Mere omission from the return of an item of receipt does neither amount to concealment nor deliberate furnishing of inaccurate particulars of income unless and until there is some evidence to show or some circumstances found from which it can be gathered that the omission was attributable to an intention or desire on the part of the assessee to hide or conceal the income so as to avoid the imposition of tax thereon. In order that a penalty under section 271(1)(iii) may be imposed, it has to be proved that the assessee has consciously made the concealment or furnished inaccurate particulars of his income."

The said principle has been reiterated in Virtual Soft Systems Ltd. v. CIT [2007] 2 Scale 612 (SC) : (2007) 289 ITR 83 (SC), where it was held (see page 97 of 289 ITR):

"24. Section 271 of the Act is a penal provision and there are well established principles for the interpretation of such a penal provision. Such a provision has to be construed strictly and narrowly and not widely or with the object of advancing the object and intention of the Legislature."

Referring to a large number of decisions, it was furthermore observed: (see page 98 of 289 ITR):

"27. Every statutory provision for imposition of penalty has two distinct components:

(i) That which lays down the conditions for imposition of penalty.

(ii) That which provides for computation of the quantum of penalty. Section 271(1)(c) and clause (iii) relate to the conditions for imposition of penalty, whereas, on the other hand,

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> Explanation 4 to section 271(1)(c) relates to the computation of the quantum of penalty.
>
> 28. The provisions of section 271 (1)(c)(iii) prior to April 1, 1976, and after its amendment by the Taxation Laws (Amendment) Act, 1975 with effect from April 1, 1976, the later provisions being applicable to the assessment year in question, are substantially the same except that in place of the word 'income' in sub-clause (iii) to clause (c) of section 271 prior to its amendment by the Taxation Laws (Amendment) Act, 1975, the expression 'amount of tax sought to be evaded' have been substituted. Explanation 4 inserted for the purpose of clause (iii) where the expression 'the amount of tax sought to be evaded', was inserted had in fact made no difference in so far as the main criteria, namely, absence of tax continued to exist, prior to or after April 1, 1976, changing only the measure or the scale as to the working of the penalty which earlier was with reference to the 'income' and after the amendment related to the 'tax sought to be evaded'. The sine qua non which was there prior to or after the amendment on April 1, 1976, was the fact that there must be a positive income resulting in tax before any penalty could be levied continued to exist. The penalty imposed was in 'addition to any tax'. If there was no tax, no penalty could be levied. The return filed declaring loss and assessment made at a reduced loss did not warrant any levy of penalty within the meaning of section 271(1)(c)(iii) with or without Explanation 4."

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10. Having regard to the findings by the ultimate fact finding authority that the assessee-Company has bona-fide belief that the services rendered by it would constitute technical services and such a bona-fide belief is also supported by the above clarification (Circular No.3 of 2004, dated 12.2.2004) issued by the Central Board of Direct Taxes, and in the light of the categorical exposition of law as to the scope and ambit of Section

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271-C of the Act in the above said judgment of the Supreme Court, the Revenue has not made out any case. We do not find any illegality or irregularity in the impugned order of the Tribunal so as to entertain this appeal. The appeal is accordingly dismissed.

Sd/-
Asst. Registrar.

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Sub Asst. Registrar.

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To

1. The Commissioner of Income Tax (Appeals) (V),
   121, Mahatma Gandhi Road, Chennai-600 034.

2. The Commissioner of Income Tax (Appeals) (XI),
   121, Mahatma Gandhi Road, Chennai-600 034.

3. The Assistant Registrar, Income Tax Appellate Tribunal,
   "B" Bench, III Floor, Rajaji Bhavan, Besant Nagar,
   Chennai-600 090.

4. The Commissioner of Income Tax, Tamil Nadu-I, Chennai.

5. The Deputy Commissioner of Income Tax
Company Circle I (3), Chennai-34.

1 cc to Ms. Pushy Sitaraman, Advocate, Sr. 71344

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