

Reassessment sets-aside as revenue didn't establish how project would be deemed as construction PE

Summary – The High Court of Delhi in a recent case of G.S. Engineering & Construction Corporation., (the Assessee) held that reassessment was required to be abandoned since reasons recorded for reassessment did not indicate as to how and why income had escaped assessment and now in view of article 5 of DTAA with Korea, concerned project was a PE.

Facts

- The assessee, a non-resident foreign company incorporated in Korea, was engaged in business of execution of construction contracts and it had five different contracts or projects in India. During the course of assessment proceedings, the assessee filed revised computation of income.
- The Director (IT) noticed that the assessee was awarded a turnkey project which involved basic and detailed engineering, construction, installation, testing and commissioning. Total amount of project was Rs. 605.34 lakh for design and detailed engineering. Out of this for engineering consultancy, an amount of Rs. 436.53 lakh was offered to tax at the rate of 15 per cent as offshore consultancy by assessee. He opined that said project was a permanent establishment as per article 5(3) and, thus, income chargeable to tax had escaped assessment and he initiated re-assessment.
- The assessee filed writ petition challenging validity of reassessment.

Held

- 'The reasons to believe' record the factual position regarding the income declared, assessment made, projects undertaken and the fact that the petitioner was a non-resident foreign company. It records that turnkey project at Haldia Refinery was awarded to the petitioner by the Indian Oil Corporation in September, 2000 and the project required engineering, construction, installation, testing commissioning, etc. The total cost of the project included Rs. 605.34 lakhs for design and detailed engineering. Engineering consultancy, from the offshore entity, amounted to Rs. 436.53 lakh which was offered as tax at the rate of 15 per cent by the petitioner in the assessment year 2002-03. The said narrations are mere statement of facts and do not make any reference to or inference regarding escapement of income. Thereafter, one single sentence is stated, that CDU project through which assessee had earned this income is a permanent establishment as per Article 5(3) of DTAA between India and Korea. Considering the above, it is evident that income chargeable to tax has escaped assessment.
- From these two sentences no one can gauge or comprehend why and on what basis it is stated that income chargeable to tax has escaped the assessment. The reasons recorded are inchoate, appear to be mere surmise and fail to clearly define why the bifurcation of Rs. 605.34 lakhs and Rs. 436.53 lakhs was relevant and *prima facie* not permissible, or how in view of Article 5(3) of DTAA this

amount should have been taxed differently. Thus, the reasons to believe relied on by the Revenue do not show why and for what reasons income chargeable to tax had escaped assessment because the CDU project through which the assessee had earned income, was a permanent establishment as per Article 5(3) of DTAA between India and Korea. They are silent and do not show any nexus and link between the facts recorded and how and why income chargeable to tax has not been taxed or under taxed. No reasonable person on reading the reasons can understand the ground why reassessment notice has been issued. In fact, they appear to be incomplete and incomprehensible, as after recording the observation that the petitioner had a permanent establishment in India, they do not indicate or state why and how the permanent establishment had adversely impacted the tax payable or income assessed in the original assessment made under section 143(3).

- The effect of reopening is to partly vacate or set aside the original order of assessment and to substitute it. Escapement of income includes both non-assessment or under-assessment but it is mandated that 'reasons to believe' must necessarily show, indicate and communicate why and for what grounds/cause any income has escaped assessment. Reasons recorded must be germane, pertinent and disclose *prima facie* belief that income has escaped assessment. Reasons to believe though subjective to this extent must satisfy this test. Relevancy of reason can be and should be established. When the reasons do not show any nexus or connection with the allegation of underassessment, they fall in the realm of suspicion, surmise and conjecture. Reasons to believe must have a rational connection and should be relevant for the formation of a belief regarding escapement of income and should not be extraneous or irrelevant, otherwise they will be considered as invalid since they do not meet the statutory preconditions/prerequisites. The policy of law is that there should be finality in all legal proceedings. Thus stale or irrelevant issues should not and cannot be a ground to reactivate closed and concluded proceedings. Formation of rational belief that income chargeable to tax had escaped assessment is a condition precedent for validly initiating reassessment proceedings.
- The language of section 147 stipulates that there should be reasons coupled with the belief and both the conditions have to be satisfied. Law requires that there should be rational connection between the reason and the belief that income chargeable to tax had escaped assessment. Reasons to believe as recorded in the present case are vague, unreasonable, incomplete and irrational. No rational or reasonable person can form or decipher from the reasons that income had escaped assessment.