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Tax law in the shadow of the higher judiciary

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Why in News:

Over the course of the last 12 months, there have been instances where the Supreme Court of India has undermined the larger commitment of Rule of Law with respect to Taxation law in India

Nature of Tax law in India

India's law of taxation is built on two central precepts.

First, on the idea captured in Article 265 of the Constitution, that a tax may be imposed only with the authority of law.

Second, on a principle of sureness that any levy ought to be clear, consistent, and predictable.

Both these precepts emanate out of a larger commitment to the rule of law, in particular to values of legality and certainty.

Upholding these principles requires a commitment not only from the legislature but also from our courts too

Role of Judiciary in Tax law

Interpretation of tax laws: Tax laws can be complex and subject to different interpretations. The judiciary is responsible for interpreting the provisions of tax laws to determine their scope, meaning, and applicability. This interpretation helps in resolving disputes and clarifying the legal framework for taxation.

Adjudication of tax disputes: When disputes arise between taxpayers and tax authorities regarding the interpretation or application of tax laws, the judiciary acts as an independent arbiter. Taxpayers can approach the courts to challenge tax assessments, claim refunds, or seek relief from penalties. The judiciary ensures a fair and impartial resolution of these disputes.

Judicial review of administrative actions: The judiciary also exercises its power of judicial review to examine the legality and validity of administrative actions taken by tax authorities. This includes reviewing the actions of tax officials, such as assessments, audits, and investigations, to ensure they are within the bounds of the law and do not violate taxpayers' rights.

Precedents and legal principles: Judicial decisions in tax cases set precedents and establish legal principles that guide future interpretations and applications of tax laws. These precedents provide clarity and consistency in tax law and help shape the overall tax jurisprudence of a country.

Constitutional scrutiny: In certain cases, the judiciary may examine the constitutionality of tax laws and tax-related provisions. This involves assessing whether the tax laws comply with the constitutional principles, such as equality, non-discrimination, and due process.

Concerns with Judicial Intervention:

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Two judgments, delivered by Justice M.R. Shah who retired from the Supreme Court on May 15, represent noteworthy examples of violating the two central precepts of tax laws in India

ITO vs Vikram Sujitkumar Bhatia Case

In the more recent of the rulings, in ITO vs Vikram Sujitkumar Bhatia, the question before the Court concerned whether an amendment to a provision of the Income Tax Act, 1961, could have retrospective effect in the absence of legislative mandate.

The provision at stake, Section 153C of the Act, which stipulates the conditions under which a search made on a person's premises could result in the opening of proceedings against other persons and entities. Before an amendment to the law in 2015, Section 153C allowed the Revenue to proceed against third parties to a search, if material seized (such as money, bullion, jewellery, or books of accounts) "belongs or belong to" a person other than the one who was subject to the search.

At least three different High Courts held that the terms, "belongs or belong to," ought to be narrowly construed. In their reading, for incriminating material found during a search to serve as a basis for assessing persons alien to the search, that material must not merely relate to, or pertain to, such person but must "belong" to them.

To overcome these decisions, the law was amended in 2015. Section 153C now stipulated that assessments could be made against third parties to a search, even if the material seized — in the case of documents and books of accounts — "pertains or pertain to" the person or if information contained in those items "relates" to the person.

The amendment was not made expressly retrospective. In any event, as the Gujarat High Court held, it could not be so because such an application would impinge on rights that had vested on persons through the previous stipulation.

This reasoning stems out of the idea that even if a law was merely procedural in nature, it would apply retrospectively only if it did not take away any substantive rights conferred on a person. Here, the Court found that the amendment was bringing into the fold of Section 153C a new class of assessee, who were previously excluded.

On April 6, the Supreme Court reversed this verdict. Its reasons for doing so, insofar as they can be gleaned from the judgment, are twofold.

One, that the old Section 153C had been replaced by amendment, and the words "belongs or belong to" had been substituted by "pertains or pertain to," and, therefore, one must presume that the unamended provision never existed in law, not even before the date of the amendment.

Two, that the new law is declaratory, in that it seeks to explain an earlier provision, and is hence retrospective.

Union of India vs Ashish Agarwal Case

In this case, the Court resuscitated notices of reassessment that had been issued by the Revenue without any sanction of law.

In doing so, it not only reversed the Allahabad High Court's judgment that had been carried to it on appeal but also verdicts rendered by at least seven different High Courts that were not before it.

Parties to those cases, numbering in the hundreds and thousands, did not so much as get their audience in court.

The issue at stake in the case was simple. With effect from April 1, 2021, Parliament had enacted a new regime to govern reassessments of completed income-tax proceedings.

But, despite the change in law, the Revenue continued to issue notices under a repealed provision, deriving authority, it believed, from executive notifications that extended timelines during the COVID-19-inflicted period.

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The High Courts declared these notices invalid, but also pointed out that the Income-Tax Department, if it so desired, was at liberty to invoke the new law, if the statute of limitation so permitted.

There is no doubt that the quashing of these notices would have had some effect on the revenue.

There would have been cases where limitation had expired, leaving the authorities with no choice but to drop any proposal for reassessment. But if this situation called for mending, it was for the legislature to think of solutions.

Instead, the Court found — although this was not the government's pleaded case — that the “officers of the Revenue may have been under a bona fide belief that the amendments may not yet have been enforced”. In other words, that state functionaries were ignorant of the law.

In the Court's belief, mistakes of this kind must not be allowed to cost the exchequer. Therefore, the quashed notices were revived, and were deemed to have been issued under the amended law.

More than an encroachment

Through this, the Court was not only encroaching on legislative functions but was also striving to give life to what were otherwise entirely illegitimate actions.

What followed the judgment was an especially bewildering situation, because the notices under the old law were evidently issued keeping in mind the preconditions that that law stipulated — as a result, this has only led to a fresh round of litigation.

What is more, in doing this, the Court also invoked its most infamous power: Article 142 of the Constitution, which allows it to pass orders for “doing complete justice to a cause”. It has previously been held that this power ought not to be applied in breach of statutory law

Yet, here was a case where the Court not only resuscitated actions that lacked any legislative support but also reversed judgments that were simply not on appeal before it.