

## Direct Tax Alert

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### Supreme Court strikes down automatic vacation of stay granted by ITAT as unconstitutional

**The Supreme Court has struck down the third proviso to section 254(2A) of the Income-tax Act, 1961 which provides for automatic vacation of stay beyond 365 days even if the assessee was not responsible for delay in hearing of the appeal**

Prior to insertion of the third proviso by the Finance Act, 2008 w.e.f. October 1, 2008, the law restricted the aggregate period of stay of demand to 365 days in cases where delay is not attributable to the assessee with a direction to the ITAT to dispose off the appeal within the said period. However, the third proviso to section 254(2A) of the Income-tax Act, 1961 ('the Act') provided for automatic and mandatory vacation of stay upon expiry of 365 days even if the delay in disposing of appeal is not attributable to the assessee.

The Supreme Court ('SC') has now ruled upon the constitutional validity of the aforementioned proviso in the case of Pepsi Foods Ltd.<sup>1</sup>. Upholding the decision of the Delhi High Court, the SC held the amendment to be both arbitrary and discriminatory and, therefore, liable to be struck down as offending Article 14 of the Constitution of India.

This alert summarises the decision of the SC.

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<sup>1</sup> DCIT v. Pepsi Foods Ltd. (Now Pepsico India Holdings Pvt. Ltd.) Civil Appeal Nos. 1106 to 1139 of 2021



## Facts of the case

The Assessee, an Indian group company of the multi-national Pepsico Inc, is engaged in manufacture and sale of concentrates, fruit juices, processing of rice and trading of goods for exports. Being aggrieved by the assessment order for AY 2008-09, it preferred an appeal before the ITAT. On 31 May, 2013, the ITAT granted stay on the assessment order which was further extended till 28 May, 2014.

Since no further extension of stay could be granted beyond the period of 365 days in view of third proviso to section 254(2A) of the Act, the Assessee, apprehending coercive action from the Revenue, filed a writ petition before the Delhi High Court challenging the constitutional validity of the third proviso.

The Delhi High Court struck down the part of third proviso which denied extension of stay beyond 365 days for no fault of assessee. Aggrieved, the Revenue had challenged this and several other judgements from various High Courts before the SC.

## Arguments by the tax department

The Revenue argued the following points:

- There is no right to obtain stay of a judgment in an appellate proceeding and the discretion to grant such stay is dependent upon the discretion of the Appellate Court.
- Discretionary remedy of a stay is part and parcel of the right to appeal which itself is a statutory right and can be taken away by the legislature.
- When Article 14 of the Constitution of India is applied to tax legislation, greater freedom must be allowed by the Courts in adjudging

constitutional validity of the same. As long as the State has laid down a valid policy which it has followed without singling out anybody, no discrimination can possibly ensue.

- Equitable considerations and arguments based on hardship are out of place when it comes to tax statutes, which must be read literally.

## Arguments by the Assessee

The following points were argued by the Assessee:

- Once discretionary relief has been granted based upon a strong prima facie case, balance of convenience, etc., it would be wholly arbitrary and discriminatory to vacate it automatically if the assessee is not at fault.
- Right to appeal inherently includes right to obtain a stay which once obtained, cannot be vacated without dilatory tactics committed on part of the Appellant.
- In the past too, discriminatory taxation has been struck down under Article 14 of the Constitution of India<sup>2</sup>.
- State cannot take shelter under a “policy”, if the policy or object laid down in the statutory provision is itself arbitrary or discriminatory.
- Though equitable considerations are not to be given effect while interpreting a tax statute, they are not wholly irrelevant when the constitutional validity of the provision is itself challenged.

## Ruling of the Supreme Court

- The SC held that appellate jurisdiction of the ITAT necessarily encompasses the power to grant stay in deserving cases to prevent the appeal from being rendered nugatory or

<sup>2</sup> Suraj Mall Mohta and Co. v. A.V. Visvanatha Sastri (1955) 1 SCR 448; Kunthath Thatehuni Moopil Nair

v. State of Kerala (1961) 3 SCR 77; Union of India v. A. Sanyasi Rao (1996) 3 SCC 465



futile<sup>3</sup>. This has, over the decades, resulted in the ITAT granting stay without being constrained by time.

- SC highlighted that challenges to tax statutes can be made under Article 14 of the Constitution of India on grounds of discrimination and manifest arbitrariness.
- Though the apparent object of section 254(2A) seems to provide for expeditious disposal of appeals, SC remarked that no differentiation is made by the third proviso between the assesseees who are responsible for delaying the proceedings and assesseees who are not so responsible thereby treating unequals also equally. SC stated that the object of the provisions itself cannot be discriminatory.
- As per the SC, discrimination is more evident when the provisions stipulating disposal of appeal by ITAT within 365 days are regarded as “directory” but so far as vacation of stay on expiry of the said period is concerned, it becomes “mandatory” for the assessee concerned.
- It observed that the section is arbitrary since vacation of stay in favour of the Revenue would ensue even if the Revenue is itself responsible for causing delay in hearing the appeal and remarked that the provision is “*capricious, irrational and disproportionate so far as the assessee is concerned*”
- It relied on another recent SC decision<sup>4</sup> which struck down the word “mandatorily” in the context of the time limit to complete IBC proceedings emphasizing the principle that an act of court shall not prejudice any man.
- In that case, the SC held that failing to abide by the prescribed time limit for no fault of the

taxpayer may result into unreasonable restriction on litigant’s fundamental right to carry on business under Article 19(1)(g) of the Constitution of India.

- Rejecting all arguments advanced and precedents relied upon by the Revenue being distinguishable to facts in the present case, the SC held the third proviso to be both 'arbitrary' and 'discriminatory' and accordingly, struck them down as transgressing Article 14 of the Constitution.
- SC remarked that the 'golden rule of interpretation' is not to be given a go-by when it comes to interpretation of tax statutes<sup>5</sup>.
- SC concluded by reading down the third proviso to section 254(2A) as, “*Any order of stay shall stand vacated after the expiry of the period... **only** if the delay in disposing of the appeal is attributable to the assessee.*”

### Dhruva Comments

This decision provides much needed respite to and instills confidence in taxpayers who were otherwise coerced by the Revenue to cough up the outstanding demand pending disposal by the ITAT without any fault of their own. It once again reiterates that tax policies cannot be arbitrary. This ruling will go a long way in restoring taxpayer’s faith and confidence in the judiciary standing up against the inequitable tax policies of the Government which violate the fundamental constitutional rights of the taxpayers.

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For any queries in relation to this tax alert, please feel free to reach out.

<sup>3</sup> Income Tax Officer v. M.K. Mohammed Kunhi (1969) 2 SCR 65

<sup>4</sup> Essar Steel India Ltd. Committee of Creditors v. Satish Kumar Gupta (2020) 8 SCC 531

<sup>5</sup> CIT v. J.H. Gotla (1985) 4 SCC 343



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