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Advance Certificate Course on Income Tax Appeal & Assessment



Revision u/s 263 & 264 - Provisions and
Procedural aspect

Background

- Sections 263 and 264 of the Indian Income Tax Act, 1961 deal with the revision of orders passed by the Assessing Officer (AO) or any subordinate authority. These sections provide a mechanism for rectifying errors or addressing issues in tax assessments that could either be
 - Prejudicial to the interest of the revenue (Section 263)
or
 - Prejudicial to the interest of the assessee (Section 264).

Legislative Intent and Objectives : Section 263

Objective:

- The primary objective of Section 263 was to empower the CIT to protect the interest of the revenue by revising erroneous orders that could result in a loss to the government. This section ensures that tax assessments are in line with the law and correct any oversight or mistakes made by the Assessing Officer (AO).

Legislative Intent:

- The legislative intent behind Section 263 was to create a supervisory mechanism where higher authorities could intervene if the lower tax officers failed to properly assess tax liabilities, thereby safeguarding the revenue.

Key Changes Over Time:

- Over the years, amendments and judicial interpretations have clarified the scope of Section 263. The courts have laid down conditions such as the necessity for the order to be both erroneous and prejudicial to revenue, ensuring a balanced approach.

Legislative Intent and Objectives : Section 264

Objective:

Section 264 was introduced to provide relief to taxpayers who felt aggrieved by an order passed by a subordinate authority. Unlike Section 263, which protects the revenue, Section 264 is designed to protect the rights of taxpayers, ensuring fairness and justice.

Legislative Intent:

The intent behind Section 264 was to offer a remedy to taxpayers who, for various reasons, may not have been able to appeal within the statutory time limit or might have been dissatisfied with the AO's order. It also allows the CIT to correct any order on their own motion, provided it is not prejudicial to the revenue.

Key Changes Over Time:

Similar to Section 263, Section 264 has evolved through judicial interpretations that have clarified its scope, including the nature of relief that can be granted and the situations where the CIT can exercise discretion.

Section 263: Revision of Orders Prejudicial to the Revenue

Power of Revision by the Principal Commissioner or Commissioner:

- **Authority:** The Principal Commissioner or Commissioner of Income Tax (CIT) can call for and examine the records of any proceedings under the Act.
- **Scope:** If the CIT considers that any order passed by the AO is erroneous and prejudicial to the interest of the revenue, they can revise the order.
- **Conditions:**
 - The order must be erroneous.
 - The order must be prejudicial to the interest of the revenue.

- **Erroneous Orders:**

- An order is deemed erroneous if it:
 - Does not follow the correct law or principles.
 - Lacks a proper inquiry by the AO.
 - Ignores relevant facts or evidence.
 - Is passed based on an incorrect interpretation of the law.

Example: If an AO passes an order granting an exemption under a wrong section of the Act, it would be erroneous.

- **Prejudicial to the Interest of Revenue:**

- An order is considered prejudicial if it results in a loss of revenue or underassessment of income.

Example: If an AO fails to disallow an expense that should have been disallowed, leading to a lower tax liability, the order is prejudicial to revenue.

Detailed Procedure

- **Initiation:**

- The CIT can initiate revision proceedings suo moto (on their own) or based on information received from the department or other sources.
- The CIT will examine the records of the assessment proceedings to determine if the order is erroneous and prejudicial to revenue.

- **Notice to the Assessee:**

- A notice is issued to the assessee, stating the grounds on which the revision is proposed. The notice must be clear and specific to enable the assessee to prepare a defense.

Hearing and Representation

The assessee has the right to be heard and can submit explanations, documents, and evidence to counter the CIT's findings.

The assessee may be represented by a Chartered Accountant, lawyer, or authorized representative.

Recording of Reasons

The CIT must record detailed reasons for considering the order erroneous and prejudicial. These reasons must be based on facts and supported by legal precedents if applicable.

Passing the Order

- After hearing the assessee, the CIT may pass an order setting aside the original assessment.
- The CIT can either: Direct the AO to make a fresh assessment.
- Modify the assessment by correcting errors.

Time Limit:

- The revision must be made within two years from the end of the financial year in which the order sought to be revised was passed.

Legal Precedents:

- **Twin Conditions:** Courts have held that both conditions—erroneous and prejudicial—must be satisfied for Section 263 to apply. If an order is erroneous but not prejudicial, or prejudicial but not erroneous, Section 263 cannot be invoked.
- **Inadequate Inquiry:** If the AO conducted an inquiry but did not gather all necessary information or failed to apply the law correctly, the CIT can invoke Section 263.
- However, if the AO made a conscious decision based on available information, the CIT cannot revise the order simply because they disagree with the AO's view.

Judicial Remedies:

- **Appeals to ITAT:** The assessee can appeal the CIT's order under section 263 to the Income Tax Appellate Tribunal (ITAT).
- The ITAT will examine whether the CIT's order meets the legal criteria and can quash it if found unsatisfactory.
- **High Court and Supreme Court:** Further appeals can be made to the High Court and the Supreme Court on substantial questions of law.

Section 264: Revision of Orders Not Prejudicial to Revenue

- **Power of Revision by the Principal Commissioner or Commissioner:**
- **Authority:** The CIT has the power to revise any order passed by an authority subordinate to him, either on the application of the assessee or on his own motion.
- **Scope:** This section applies to orders that are not prejudicial to the revenue but are potentially prejudicial to the assessee.
- **Conditions:**
 - The order may be erroneous, but it need not be prejudicial to the revenue.
 - The application for revision must be made within one year from the date on which the order was communicated to the assessee or the date on which the assessee came to know about the order, whichever is earlier.

Time Limit and Conditions:

- Filing of Application: The application must be filed within one year from the date of the order's communication or the date when the assessee first became aware of the order.
- However, the CIT has discretion to admit a delayed application if there is a reasonable cause for the delay.

Restrictions:

- The CIT will not revise an order:
- Where the assessee has a right of appeal but did not file one. Where the appeal has been filed but withdrawn.
- Where the application for revision is made after the expiry of the statutory period unless condoned by the CIT.

Finality and Judicial Recourse:

- **Finality of the Order:** The order passed under Section 264 is final. The assessee cannot appeal against this order in the ITAT.
- However, the order can be challenged before the High Court through a writ petition under Article 226 of the Constitution of India if it involves questions of law or if the order is arbitrary, discriminatory, or beyond the jurisdiction of the CIT.
- **Relief and Rectification:** If the CIT finds that the assessee is entitled to relief, they can pass an order granting such relief, including a refund of taxes paid.

Judicial Precedents:

- CIT's Discretion: Courts have upheld that the CIT has wide discretion under Section 264. However, this discretion must be exercised judiciously and fairly, keeping in mind the principles of natural justice.
- Writ Jurisdiction: The High Courts have intervened in cases where the CIT's order under Section 264 was found to be arbitrary or where the CIT failed to consider material facts or legal principles.

Practical Considerations:

Strategic Use of Section 264:

Assessee often use Section 264 to seek relief in cases where the tax impact is small and an appeal may not be cost-effective or time-efficient. It can also be used to correct minor errors without entering into prolonged litigation.

Documentation and Evidence:

It is crucial for the assessee to maintain thorough documentation and evidence when applying under Section 264. The application should clearly articulate the error or grievance and provide supporting documents to justify the revision.

Risk of Section 263:

From a tax planning perspective, assessee must be aware of the risks associated with Section 263. Orders passed by the AO that involve significant tax benefits or aggressive tax positions should be reviewed carefully to ensure they are robust against potential revision by the CIT.

Summing up

- Sections 263 and 264 of the Income Tax Act provide important mechanisms for revising orders passed by the AO, serving both the interests of the revenue and the taxpayer. Understanding the nuances of these sections is essential for effectively managing tax disputes and ensuring that tax assessments are fair, accurate, and legally sound.





THANK YOU!