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Court : Gujarat

Decided On : Mar-10-2008

Reported in : [2008]307ITR83(Guj); [2009]176TAXMAN416(Guj)

Judge : D.A. Mehta and; Z.K. Saiyed, JJ.

Appellant : CiT

Respondent : Mehsana Dist. Co-Operative Milk Producers' Union Ltd.

Judgement :

D.A. Mehta, J.

1. Though the cause title shows revenue being the applicant in fact there are cross-references, both by the assessee and the revenue.

2. The Tribunal, Ahmedabad Bench 'B', has raised and referred the following question under Section 256(1) of the Income Tax Act, 1961 (the Act) at the instance of the CIT:

Whether the Tribunal is right in law and on facts in confirming the order made by the Commissioner (Appeals) deleting the addition of Rs. 6,02,03,652 representing the alleged additional price of milk, paid to the member co-operative societies on the last day of the accounting year

3. It is an admitted position between the parties that identical issue had come up in the assessee's own case for immediately preceding year and the issue now stands concluded by virtue of the judgment rendered in case of CIT v. Mehsana District Co-operative Milk Producers Union Ltd. (2005) 195 CTR (Guj) 385 : (2006) 282 1TR 24 (Guj). Hence, for the reasons stated in judgment rendered on 24th Feb., 2005 between the same parties, the question referred, at the instance of the revenue is required to be answered in the affirmative i.e., in favour of the assessee and against the revenue.

4. The Tribunal has also referred following two questions at the instance of the assessee:

1. Whether on the facts and in the circumstances of the case, the Tribunal was right in law in holding that the amount transferred to reserve fund account as per provisions of Section 67 of Gujarat Co-operative Societies Act, 1961 was not a diversion of income at source by overriding title; ?

2. Whether on the facts and in the circumstances of the case, the Tribunal was right in law in holding that the transfer to reserve fund cannot be treated as a business expenditure and allowed deduction under Section 28/37 of the Income Tax Act, 1961 ?

5. Mr., M.J. Shah, learned advocate for the applicant assessee, has submitted that the Tribunal has followed its own order for asst. yrs.1983-84 to 1986-87 in the present case, which relates to assessment year 1987-88 and hence, connected reference, at the instance of the assessee, being IT Ref. No. 86 of 1996 has also been heard together wherein identical two questions have been raised and referred for the opinion of this Court.

6. It was submitted on behalf of the applicant assessee that Section 67 of the Gujarat Co-operative Societies Act, 1961 (the Co-operative Societies Act)requires every society to maintain a reserve fund where the society derived or can derive profits from the transactions carried on by the society. For the purposes of constituting such a reserve fund, according to Mr. Shah, under Sub-section (2) of Section 67 of the Co-operative Societies Act,at least one-fourth of the net profits of

the society are required to be carried to the reserve fund every year, but such reserve fund is not a free fund and hence, before the profits are transferred to the reserve fund at the appropriate rate there is a diversion at source by virtue of provisions of Section 67 of the Co-operative Societies Act which operates as an overriding title. Hence, it was submitted that the amount transferred to the reserve fund cannot be charged as income liable to tax under the Act. Alternaavely it was pleaded that the amount of profits transferred to the reserve fund would constitute a charge on the taxable income under provisions of Section 28 of the Act, or an expenditure having the characteristic of business expenditure under Section 37 of the Act, and thus not liable to be taxed, being a deductible expenditure. Itwas submitted that the proviso under Sub-section (2) of Section 67 of the Cooperative Societies Act granted powers to the Registrar of the Cooperative Societies to lower the limit to one-tenth of the net profits for the purposes of transferring to reserve fund but at all stages the amount transferred to the reserve fund was liable to be invested as directed by the State Government and was also liable to be utilized for some public purpose likely to promote the objects of the Co-operative Societies Act or for any other purpose of the State akin to promoting the co-operative movement or of local interest. In other words, the contention was, the assessee was divested over the domain of the fund once the amount was transferred to the reserve fund and, therefore, the amount so carved out from the profits of the society was an outgoing insofar as the society was concerned and hence, being a statutory expense, was an allowable deduction. In support of the submissions reliance was also placed on Section 115 of the Co-operative Societies Act.

7. As against that on behalf of the revenue Mr. M.R. Bhatt, learned senior standing counsel, invited attention to the apex court decision in the case of Associated Power Co. Ltd. v. CIT : [1996]218ITR195(SC) , to submit that in similar situation, merely because there is a statutory liability to transfer a part of the profits neither can the profits be exempted from tax on the ground of diversion at source by overriding title nor can such amount be treated as a deductible expenditure.

8. Having heard the learned advocates it is apparent that the issue raised by the two questions, at the instance of the assessee, stands concluded by the aforesaid

decision of the apex court in the case of Associated Power Co. Ltd. v. CIT (supra). Furthermore, as can be seen from provisions of Section 67(2) of the Co-operative Societies Act, the question of control of the State Government by specifying the mode of investment or the mode of use of the reserve fund can arise only in the eventuality when the society does not use the reserve fund in the business of the society. The opening portion of Sub-section (2) of Section 67 of the Co-operative Societies Act specifically provides '...and such reserve fund may be used in the business of the society or '. In other words, it is only in the event the society does not choose to use the reserve fund for the business of the society that the question about investing the reserve fund in the specified category of investments and thereafter utilizing the same for the objects specified by the State Government can arise. Hence, not only is there no diversion of income by overriding title but in fact there is no outgoing of funds from the domain of the assessee society. In fact, the profits affhe specified percentage are set apart so as to be available to the society for use in the business of the society at a later point of time. Once the society is in a position to use the funds lying in the reserve fund for the business of the society as and when the society so chooses, there can be no question of keeping out such profits from the purview of taxation.

9. Accordingly, the Tribunal was right in law in holding that the amount transferred to the reserve fund account as per provisions of Section 67 of the Gujarat Co-operative Societies Act, 1961, was not diversion of income at source by overriding title nor can such transfer be treated as a business expenditure deductible either under Section 28 or Section 37 of the Act. Accordingly, both the questions at the instance of the assessee are answered in the affirmative i.e., in favour of the revenue and against the assessee.

10. The reference stands disposed of accordingly. There shall be no order as to costs.

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