

Daga and Co. (P.) Ltd. Vs. Commissioner of Income-tax

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Court : Kolkata

Decided On : Feb-14-1990

Reported in : [1997]227ITR480(Cal)

Judge : Suhas Chandra Sen and ;Bhagabati Prasad Banerjee, JJ.

Acts : [Income Tax Act, 1961](#) - Section 40A(8)

Appeal No. : Income-tax Reference No. 148 of 1985

Appellant : Daga and Co. (P.) Ltd.

Respondent : Commissioner of Income-tax

Advocate for Def. : A.N. Bhattacharjee, Adv.

Advocate for Pet/Ap. : Kalyan Roy and ;R.N. Datta, Adv.

Judgement :

S.C. Sen, J.

1. The Tribunal has referred the following question of law under Section 256(1) of the Income-tax Act, 1961 ('the Act') :

' Whether, on the facts and in the circumstances of the case, the Tribunal was correct in holding that the interest paid by the assessee-company was in respect of deposits received by it and, as such, 15 per cent. thereof was not allowed as deduction under Section 40A(8) of the Income-tax Act, 1961 ?'

2. The relevant assessment year is 1982-83, for which the year of accounting was 1981-82.

3. The Tribunal has stated the following facts set out in the statement of the case :

' The assessee-company is admittedly neither a banking company nor a financial company. It claimed to have had incurred an expenditure of Rs. 99,320 by way of interest in respect of moneys received by it. The Income-tax Officer disallowed Rs. 14,989 under Section 40A(8) of the Act being 15 per cent. of Rs. 99,320,

The assessee took up the matter in appeal before the Commissioner (Appeals). Its contention before the Commissioner (Appeals) was that out of Rs. 99,320, Rs. 93,247 was paid as interest to Amit Kumar Daga, Godavari Devi Daga, Lila Bhoopal, Sunil Kumar Daga and others, Bhagwan-das Daga and others, Bhawandas Daga and Bansidhar Sitaram and Co., who were directors, their relatives and firms in which they were interested. The credits in their accounts, the assessee-company took a stand, could not be considered to be 'deposits' within the meaning of Section 40A(8) of the Act. The plea of the assessee found favour with the Commissioner (Appeals). He accordingly deleted the disallowance of interest paid to these persons. The Department came up in appeal before the Tribunal. The Tribunal, following its earlier order dated July 27,

1984, in the cross-objection Nos. 148 to 150 (Cal) of 1982 in I.T.A. Nos. 2124 to 2126 (Cal) of 1982 relating to the assessment years 1979-80 to 1981-82 filed by the assessee allowed the Department appeal by the order under reference.'

4. The Tribunal's order in the appeals relating to the assessment years 1979-80 to 1981-82 is also the subject-matter of another reference which is appearing in the cause list today marked as Income-tax Reference No. 111 of 1985. Both these cases were heard together because common questions of fact were involved.

5. The Tribunal in its order for the assessment years 1979-80 to 1981-82 has dealt with the problem in the following manner :

' The assessee is a company. As per details furnished in the paper book by the assessee, the following amounts of interest were paid to certain persons named below, 15 per cent of which, viz., Rs. 23,146, Rs. 21,822, Rs. 20,292 + Rs. 1,530 and Rs. 17,184 (Rs. 16,674 + Rs. 510) in the assessment years 1979-80 and 1981-82, respectively, have been disallowed under Section 40A(8) of the Income-tax Act (for brevity the Act) by the Income-tax Officer :

Name Assessment year 1979-80

(Rs.) Assessment year 1980-81

(Rs.) Assessment year 1981-82

(Rs.)

Puspa Devi Sarada	1,549.00	--Bansidhar Sitaram and Co.	58,545.00	19,783.00	43,550.00	Anandi Devi					
Kalyani	308.00	333.00	359.00	Amit Kumar Daga	1,419.00	1,268.00	1,438.00	Dadawari Devi			
Daga	25,278.60	23,615.72	24,220.59	Kamala Devi	3,090.00	3,312.00	3,351.00	Lila			
Bhorpal	8,893.70	13,522.00	14,842.37	Mathura Devi	42.00	36.00	--Saraswati Devi				
Kalyani	2,116.00	2,865.00	2,428.98	Sarda and other	9.00	--Shanti Devi Hijawar	215.00	233.00	251.00	Sunil Kumar	
Daga and others	9,284.00	3,197,001,962.00	Bhagwandas Daga and others	22,381.87	24,558.00	26,501.75	Bhagwandas Daga	20,868.86	16,869.00	16,189.59	S. K. Daga and others
	173.63	1,54,312.00	1,11,165.00	1,35,284.00							

Such disallowance has been maintained by the Commissioner(Appeals) in the appeals for all the three years. According to the tax authorities below 15 per cent. of such expenditure towards the payment of interest was not allowable deduction.

The contention of counsel for the assessee is that the interest was paid on the current account of the directors of the company and their relatives and friends- Such payment does not fall within the mischief of Section 40A(8) of the Act. Reliance was placed upon orders of 'C' Bench of the Tribunal at Madras in Income-tax Appeals Nos. 444 to 446 (Mad) of 1981, dated February 19, 1982 in the case of Shivraj Motors Ltd. v. ITO and order dated February 2, 1980, of 'B'

Bench of the Tribunal at Bombay in Income-tax Appeal No. 691 (Bom) of 1979 in the case of M. E. (P.) Ltd. v. ITO [1981] 11 TEJ (Bom) 299. He also placed reliance upon the order of the Commissioner (appeals)-XI, Calcutta, dated March 3, 1983, in the case of this assessee-company itself for the assessment year 1982-83.

The learned Departmental Representative, on the other hand, argued that the principal amounts on which interest was paid to different persons, were none the less deposits within the meaning of Explanation (b) to Section 40A(8) of the Act and such deposit does not find place in the list of exemptions given in the said Explanation, He, therefore, vehemently opposed the cross-objections and supported the orders of the Income-tax Officer and the Commissioner (Appeals).

A minute analysis of Section 40A(8) and the meaning of 'deposit' shows that interest paid on any deposit or

loan except those enumerated in Explanation (b) comes within the restrictions placed by the section. 'Deposit' has been defined as any deposit of money with the company and it also includes any money borrowed by the company. Thus, 'deposit' has a wide meaning and it takes into its amplitude any money received by the company as deposit or loan. It does not make any exception of the directors, their relatives and friends as the creditors. However, the meaning of 'deposit' cannot be extended to any such transaction which is neither deposit nor loan, e.g., if any businessman or director has many dealings with the company in the course of business of the company and on that account if interest has been paid, it does not come within Section 40A(8) of the Act. In this sense as we understand it has been held by the Benches of the Tribunal at Madras and Bombay that interest paid on current accounts is entitled to be deducted in full. The orders of the two Benches of the Tribunal cannot be spelled out to mean that the interest paid on the deposits to the directors of the company and their relatives and friends, is allowable in full. Those two orders make a distinction between deposits' and current accounts. Such distinction cannot be made to restrict to the directors of the company and their relatives and friends. Interest paid to any person is entitled to be deducted in full if it is paid on a current account and it does not fall within the meaning of deposit.

Thus, the crucial point for determination in this case is as to whether the amounts on which interest was paid by the assessee-company in all these three years were deposits or were the cash credits in the current account or in the course of business of the company. To constitute a current account or an account in the course of business of the company, there must be a transaction each side creating an independent obligation on the other. Mere credit entries with adjustment entries like payments of interest and deduction of tax at source cannot make an account a current account or an account in the course of business transaction. Such account cannot be taken out of the ambit of the word 'deposit'. Since the assessee claimed deduction in full, the burden lay on it to prove that the interest was not paid on deposits. The assessee-company has filed copies of accounts of the persons payment of interest to whom is in question. A minute examination of these accounts shows that they were not current accounts. There are credit entries of cash balance and the amount of interest accrued and also the amounts of dividends received from, other companies. On the debit side, only payment to certain persons on their behalf, viz., to the Life Insurance Corporation, the Municipal Corporation, etc., and tax deducted at source appeared. Such account by no stretch of imagination can be taken as current account. We have minutely gone through the copies of the accounts of the creditors filed in the paper book and we do not find that any of the accounts can be taken as current account. It is not known as to in what capacity Bansidhar Sitaram and Co. had transactions with the assessee-company. In the accounts of that company there are many items of withdrawals but they have not been proved as being out of the ambit of deposit.'

6. Mr. Roy appearing on behalf of the assessee contended that the Tribunal has misunderstood the meaning of the word 'deposit' employed in Section 40A(8) of the Act. He has contended that it is not necessary specifically to go into the Explanation provided by the statute. The amounts standing to the credit of the shareholders and directors were nothing but accounts maintained by the company. Moneys were paid into these accounts and were also disbursed from these accounts. Therefore, these accounts cannot be treated as deposit accounts.

7. Secondly, it was contended that the company had obtained loans and paid interest to a large number of persons. In those cases, the company had no grievance on account of applicability of Section 40A(8) but in the case of directors and other persons connected with the company the Tribunal has failed to appreciate the nature of the accounts maintained by these persons in the company.

8. Lastly, our attention was drawn to a judgment of the Madhya Pradesh High Court in the case of CIT v. Kalani Asbestos (P.) Ltd. : [1989]180ITR55(MP) . In that case the Tribunal had found that interest was not paid by the assessee-company in respect of any deposit received by it. The Madhya Pradesh High Court held that the Tribunal was right in holding that disallowance under the provisions of Section 40A(8) was not called for.

9. In the instant case, the finding of the Tribunal is that the interest was paid by the assessee in respect of the

deposits received by it. Therefore, the provisions of Section 40A(8) will be clearly attracted.

10. Section 40A(8) provides as follows :

'40A. (8) Where the assessee, being a company (other than a banking company or a financial company), incurs any expenditure by way of interest in respect of any deposit received by it, fifteen per cent. of such expenditure shall not be allowed as a deduction.

Explanation.--In this sub-section,-- . . .

(b) 'deposit' means any deposit of money with, and includes any money borrowed by, a company, but does not include any amount received by the company-

(i) from the Central Government or any State Government or any local authority, or from any other source where the repayment of the amount is guaranteed by the Central Government or a State Government ;

(ii) from the Government of a foreign State, or from a citizen of a foreign State, or from any institution, association or body (whether incorporated or not) established outside India ;

(iii) as a loan from a banking company or from a co-operative society engaged in carrying on the business of banking (including a cooperative land mortgage bank or a co-operative land development bank) ;

(iv) as a loan from any institution or body specified in the list in the Tenth Schedule or such other institution or body as the Central Government may, having regard to the nature and objects of the institution or body, by notification in the Official Gazette, specify in this behalf ;

(v) from any other company ;

(vi) from an employee of the company by way of security deposit ;

(vii) by way of security or as an advance from any purchasing agent, selling agent or other agent in the course of, or for the purpose of, the business of the company or as advance against orders for the supply of goods or for rendering of any service ;

(viii) by way of subscription to any share, stock, bond or debenture (such bond or debenture being secured by a charge or a lien on the assets of the company) pending the allotment of the said share, stock, bond or debenture, or by way of advance payment of any moneys uncalled and unpaid upon any shares in the company, if such moneys are not repayable in accordance with the articles of association of the company ;

(ix) as a loan from any person where the loan is secured by the creation of a mortgage, charge or pledge of any assets of the company (such loan being hereafter in this sub-clause referred to as the relevant loan) and the amount of the relevant loan, together with the amount of any other prior debt or loan secured by the creation of a mortgage, charge or pledge of such assets, is not more than seventy-five per cent. of the price that such assets would ordinarily fetch on sale in the open market on the date of creation of the mortgage, charge or pledge for the relevant loan ; '

11. It will appear from Section 40A(8) that expenditure incurred by way of interest by an assessee shall not be allowed as a deduction in its entirety. 15 per cent. of such expenditure will have to be disallowed if the interest was paid 'in respect of any deposit received by it'. The word 'deposit' has been explained to mean any deposit of money with, and includes any money borrowed by a company. There are some specific exclusions in Sub-clauses (i) to (ix) in Explanation (b). The sub-clauses do not apply specifically to the instant case. But the definition goes to indicate that not only money borrowed by a company but also moneys deposited with a company are to be treated as deposit.

12. Mr. Roy has contended that the word 'borrowing' has got a definite connotation. There is no difficulty in

upholding this contention. But the provisions of Section 40A(8), Explanation (b), are not limited to borrowings. Assuming that the company did not borrow the money, the question will still remain whether the amounts that were lying with the company in the accounts of the directors and other shareholders were moneys deposited with the company.

13. The main difficulty in the way of the assessee in this case is that the assessee has not established the facts to get out of the scope and ambit of Section 40A(8) at all. It was for the assessee to prove how these alleged accounts came into existence and when the directors and shareholders of the company started depositing money with the company. Mr. Roy submitted that the company might have run into financial trouble and the directors and shareholders interested in the company might have helped out the company with money. But that is not a fact found by the Tribunal.

14. Mr. Roy has referred us to the accounts that were lying with the company and has tried to argue that there were both debit and credit entries in these accounts. It will appear from the various accounts that large sums of money were lying to the credit of the various parties. Some moneys were paid out of these accounts to discharge personal or statutory obligation of the depositors.

15. One of the accounts annexed to the statement of case is the ledger account of Amit Kumar Daga, which is set out below :

'IN ACCOUNT WITH DAGA AND CO. PVT. LTD. JALPAIGURI FROM 1-4-1981 TO 31-3-1982

Date Particulars Dr. Cr. Balance

1981-82 April 1 By Balance 12,356.00 March 31 By Interest up to 31-3-1982 1,606.00 To Income-tax on interest 161.00 To Balance 13,801.00

Cr. 13,801.00 13,962.00

13,962.00

1982-83 April 1 By Balance 13,801.00 FOE DAGA AND Co. PRIVATE LTD.'

16. The credit entry of Rs. 1,606 was on account of interest payable on the sum of Rs. 12,356 which was the opening balance of account on September 14, 1981. The only debit entry in the account is of a sum of Rs. 161 which has been deducted at source for payment of income-tax.

17. There is an account of one Lila Pal of which the opening entry was Rs. 1,35,638.27. Dividend amount of Rs. 92.04 and interest of Rs. 16,340.62 were credited to this account. A sura of Rs. 1,634 has been deducted at source on account of income-tax payable on the amount of interest. The Tribunal is right in concluding that this is not a business account maintained by a party with the company. The Tribunal has held that there are no cross-entries in this account. The Tribunal is right in its conclusion that the debit entries were really made to discharge the statutory obligations.

18. Counsel on behalf of the assessee referred us to the balance-sheets of the company. The balance-sheets indicate that the company was not in need of any loan. The company's subscribed share capital was shown in the balance-sheet as Rs. 14,87,000. It appears that 3,800 ordinary shares of Rs. 500 were issued at only Rs. 365 each. The reserve and surplus account of the company stood at more than Rs. 62 lakhs. The company had also advanced large amounts by way of loan. It could also not be explained why this full amount of Rs. 500 per share was not realised in spite of the alleged financial difficulties of the company.

19. There is nothing to indicate that these accounts of the directors and their associates were current business accounts of the company with its business associates. In such a case there would have been the cross-entries of debit and credit between the company and the account-holder. The only debit entries in the accounts were in respect of statutory payments made to the Government or to the Life Insurance

Corporation. There are no mutual transactions between the assessee-company and the depositors. The findings of fact made by the Tribunal have not been challenged as perverse.

20. In view of the above, the question is answered in the affirmative and in favour of the Revenue.

21. There will be no order as to costs.

Bhagabati Prasad Banerjee, J.

22. I agree.

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