

(2003) 09 KL CK 0052

In the High Court Of Kerala

Case No : IT Ref. No. 12 of 2000 & IT Ref. No. 12 of 2000 1 September 2003

Commissioner of Income Tax

APPELLANT

Vs

J. Rajmohan Pillai

RESPONDENT

Date of Decision : 01-09-2003

Acts Referred:

Income Tax Act, 1961 — Section 40A(3)
Income Tax Rules, 1962 — Rule 6DD

Citation : (2004) 186 CTR 296 : (2004) 267 ITR 561

Hon'ble Judges : J.M. James, J;G. Sivarajan, J

Bench : Division Bench

Advocate : P.K.R. Menon and George K. George, for the Appellant; P. Balachandran and Preetja S. Nair, for the Respondent

Judgement

G. Sivarajan, J.—The Tribunal, Cochin Bench at the instance of the Revenue has referred the following question of law as per direction issued by this Court in the judgment dt. 5th Oct., 1999, in O.P. No. 22075 of 1999 for decision by this Court:

"Whether, the Tribunal was justified in holding that the provisions of Rule 6DD(j) of the IT Rules apply to the facts of the case, vis-a-vis Section 40A(3) of the IT Act?"

2. The brief facts are as follows : The assessee is an exporter of cashew kernels. The assessee, during the previous year relevant to the asst. yr. 1990-91, had purchased raw cashewnuts from various places including the State of Orissa and the same was transported to the assessee's factories in Kanyakumari for processing. In the assessment for the year 1990-91 the assessee claimed deduction of a total sum of Rs. 10,98,698 as transport and coolie charges for transporting raw cashewnuts. The AO held that out of the said expenses payment of Rs. 10,28,350 had to be subjected to the provisions of Section 40A(3) of the Act as the payments were made otherwise than by way of crossed cheques or bank drafts. Since the assessee had effected payment of the said amount in cash in violation of the provisions of Section 40A(3) the said amount was disallowed.

In appeal filed by the assessee, the CIT(A) upheld the said disallowance stating that the assessee has not proved that the said payment will come within the exclusionary provisions of Rule 6DD(j) of the IT Rules. In further appeal by the assessee the Tribunal allowed the claim. Hence the reference.

3. We have heard Sri P.K.R. Menon, learned senior counsel (Government of India) Taxes appearing for the applicant, and Sri P. Balachandran, learned counsel appearing for the respondent. The senior counsel submitted that in regard to the payment of Rs. 10,28,350 towards transportation and coolie charges, admittedly the payments were made otherwise than by way of crossed cheques or bank drafts and, therefore, the provisions of Section 40A(3) were applicable. The senior counsel further submitted that since the assessee was not able to substantiate by evidence that the proviso to Section 40A(3) r/w Rule 6DD(j) of the Rules applied to exclude the applicability of the main part of Section 40A(3) the said amount was rightly disallowed by the AO and confirmed by the first appellate authority. The senior counsel submitted that the Tribunal had committed a serious error in allowing the claim by holding that the circumstances stated by the assessee would definitely be an exceptional or an unavoidable circumstance to make the payment eligible for exclusion under Clause (i) of Rule 6DD(j). The senior counsel submitted that the assessee had not established that the present case would fall under the exclusionary clause contained in Rule 6DD(j) of the Rules. On the other hand, the contention of the counsel for the assessee is that the AO has not doubted the genuineness of the transport of raw nuts from Orissa to Kanyakumari District as also the identity of the transporter and the payment of the charges. He further submitted that the only circumstance pointed out for rejecting the claim is that the assessee had not produced evidence obtained from drivers of the vehicles in which the raw cashewnuts were transported during the relevant period to the effect that they insisted for payment of the transport and coolie charges in cash. The counsel further submitted that it was impracticable for obtaining bank drafts or for issuing crossed cheques to the transporting company or to the drivers of the vehicle at the time of purchase and that the transporting agency/drivers had insisted for payment of the transporting charges and coolie charges in cash and the assessee had no option but to pay the amount in cash having regard to the commercial expediency. He further submitted that the assessee could not get confirmation letters from the truck drivers to whom the payments were made to the effect that they had insisted for payment in cash only since they could not be contacted at a later stage. The counsel further submitted that the Tribunal, the final fact-finding authority, considering the totality of circumstances had accepted the explanation of the assessee and had held that the assessee had satisfied the exclusionary provisions of Clause (i) of Rule 6DD(j). The counsel on that basis submitted that no question of law does arise from the order of the Tribunal requiring adjudication by this Court.

4. We have considered the rival submissions and had also perused the orders of the AO and the two appellate authorities. The AO had noted that the assessee

had made 16 payments in cash above Rs. 10,000 for a total amount of Rs. 10,63,350 mostly for transporting charges and gunny bag purchase. The assessee had explained before the officer that the lorry drivers and secondhand gunny bag dealers will not accept cheques. The AO referred to two decisions of the Andhra Pradesh High Court regarding the scope of Rule 6DD(j) of the Rules which held that a mere assertion that the recipient was unwilling to accept payment by cheque is not sufficient, but the assessee had to furnish evidence to establish this point and that after establishing the existence of a genuine difficulty the assessee must then furnish evidence of the identity of the payee and genuineness of the transaction. The assessing authority then observed that in the instant case the assessee had not established any of the above points. The CIT(A) noted that on an earlier occasion he had remanded the matter to the AO to verify the genuineness of the bills and cash receipts produced by the assessee and also to allow the appellant an opportunity to produce necessary evidence from the company regarding their insistence on cash payment. It was also noted that the assessee had later produced the bills and the receipts issued by the Kerala Road Transport Co. but did not furnish any evidence from the company regarding their insistence on cash payment. The CIT(A) then noted that although the identity of the payee and genuineness of the transactions have been established, the assessee has not proved that the assessee had been forced to make the payment in cash. It was also observed that there is no use in arguing that the lorry drivers insisted for payment in cash and the ultimate beneficiary of the payment were not the lorry drivers but the transporting company, i.e., the K.T.C. It was further observed that K.T.C. is a reputed concern with offices and depots all over India and its headquarters in Kerala itself and that there is absolutely no reason why they would have refused to accept the crossed cheques or crossed D.D. from the appellant who himself was a very leading and reputed dealer in his line of business. With these observations the first appellate authority held that the assessee had not discharged his burden of proof that his case will fall under the exclusionary provisions of Rule 6DD(j). The Tribunal had considered the contentions of the assessee and the Department in paras 3 and 4 of the appellate order and then observed as follows :

"We have given due consideration to the submissions on both sides and gone through the facts of the case. The assessee was making payment to the truck drivers who were transporting raw cashewnuts from Orissa to Kanyakumari District in Tamil Nadu. The assessee's claim is that the drivers would not accept crossed cheque or demand drafts and that they insisted on the payment in cash only. It was submitted by the learned representative of the assessee, that by the time the assessment was made, it was not possible to contact the truck drivers and get letters of confirmation from them to the effect that they had insisted on the payment in cash only. If the assessee had to make the payments in cash to the drivers even though ultimately the money reached Kerala Road Transport Co., it would not be correct to say that the assessee's case does not fall within the exceptional clause in Rule 6DD(j). Rule 6DD(j) provides that no disallowance

shall be made in a case where the assessee satisfies the AO that the payment could not be made by crossed cheques or bank drafts due to exceptional or unavoidable circumstances. If the truck drivers who were transporting raw nuts from Orissa to the assessee's factories in Kanyakumari District insisted on the payment in cash, that would definitely be exceptional or unavoidable circumstance to make the payment eligible for exclusion under Clause (i) of Rule 6DD(j). The genuineness of the payment has not been disputed by the Revenue authorities. The fact that the assessee had got the raw nuts transported in the trucks belonging to Kerala Road Transport Co. was also not disputed. The learned representative of the assessee has explained the reason why the assessee could not get evidence or confirmation letters from the truck driver to whom the payment was made. In exceptional and unavoidable circumstances, if the assessee had to make the payment in cash, we are of the view that such payments could not be disallowed u/s 40A(3). For this view of the matter, we also find support in the decision of the Tribunal (Delhi Bench) in the case of Nuchem Plastic Ltd. v. Dy. CIT (1992) 44 TTJ (Del) 261. In the above circumstances, we delete the disallowance of Rs. 10,28,350 in the computation of the total income."

5. Section 40A of the Act deals with expenses or payments not deductible in certain circumstances. Sub-section (3) thereof as it stood at the relevant time provides that where the assessee incurs any expenditure in respect of which payment is made, in a sum exceeding ten thousand rupees otherwise than by a crossed cheque drawn on a bank or by a crossed bank draft, such expenditure shall not be allowed as a deduction. Here, it must be noted that as per Finance (No. 2) Act, 1996 the words "ten thousand rupees" were substituted by "twenty-five thousand rupees" w.e.f. 1st April, 1997. Thus, at the relevant time (asst. yr. 1990-91) the limit was ten thousand rupees. Further, the words "such expenditure shall not be allowed as a deduction" were substituted by the words "twenty per cent of such expenditure shall not be allowed as a deduction" by the Finance Act, 1995 w.e.f., 1st April, 1996. However, the second proviso to Sub-section (3) states that no disallowance under this sub-section shall be made where any payment in a sum exceeding ten thousand rupees is made otherwise than by a crossed cheque drawn on a bank or by a crossed bank draft in such cases and under such circumstances as may be prescribed having regard to the nature and extent of banking facilities available, consideration of business expediency and other relevant factors. It is by virtue of the second proviso to Sub-section (3) Rule 6DD is framed. The said rule deals with cases and circumstances in which payment in a sum exceeding ten thousand rupees may be made otherwise than by a crossed cheque drawn on a bank or by a crossed bank draft. Clause (j) of the said rule which is relevant for the purpose of this case reads thus:

"In any other case, where the assessee satisfies the AO that the payment could not be made by a crossed cheque drawn on a bank or by a crossed bank draft--

(1) due to exceptional or unavoidable circumstances, or

(2) because payment in the manner aforesaid was not practicable, or would have caused genuine difficulty to the payee, having regard to the nature of the transaction and the necessity for expeditious settlement thereof, and also furnishes evidence to the satisfaction of the AO as to the genuineness of the payment and the identity of the payee."

The aforesaid rule would reveal that it sets out four circumstances in which the rigour of the provision contained in Sub-section (3) has to be relaxed, namely, where the assessee satisfies the ITO that the payment could not be made by crossed cheque or by crossed bank draft due to (1) exceptional circumstances, (2) unavoidable circumstances, (3) it was not practicable having regard to the nature of the transaction and the necessity for expeditious settlement thereof, and (4) it would have caused genuine difficulty to the payee having regard to the nature of the transaction and the necessity for expeditious settlement thereof. The assessee has to further satisfy the AO by furnishing evidence regarding the genuineness of the payment and the identity of the payee. The existence of exceptional or unavoidable circumstances is a question of fact, Circular No. 220, dt. 30th May, 1977, issued by the CBDT gives some of the circumstances in which the provisions of Rule 6DD(j) would be attracted. Some of the circumstances mentioned in the circular which are relevant for the purpose of this case are (1) the purchaser is new to the seller, (2) the transactions are made at a place where either the purchaser or the seller does not have a bank account, (3) the transactions and payments are made on a bank holiday, (4) the seller is refusing to accept the payment by way of crossed cheque/draft and the purchaser's business interest would suffer due to non-availability of goods otherwise than from this particular seller. As held by the Allahabad, Delhi, Punjab & Haryana High Courts in Commissioner of Income Tax Vs. Satish Chandra, , Commissioner of Income Tax, Delhi-VI Vs. Union Agencies, and in Commissioner of Income Tax Vs. Sawaran Singh Balbir Singh, existence of exceptional or unavoidable circumstances is a question of fact. The scope and content of the provisions of the second proviso to Section 40A(3) and Rule 6DD(j) was very elaborately considered by the Gujarat High Court in Hasanand Pinjomal Vs. Commissioner of Income-tax, Gujarat, .

6. Regarding the scope of Rule 6DD(j) it was observed as follows:

"The legislature found from experience that the existing provisions of the Act were inadequate to deal with evasion of tax under the cloak or guise of permissible deductions and also that many payments were made with unaccounted money possessed by the assessee and deductions were claimed in respect of such payments. In order to remedy such situation, Section 40A was added by the Finance Act of 1968 and it came into force w.e.f. 1st April, 1968. While introducing the Bill in the Lok Sabha for its consideration, the Finance Minister made a speech on 29th April, 1968, in which he pointed out that the provision in question was intended to serve the objective of checking tax

evasion. Though the Finance Minister did not elaborate, it is obvious that the intention of the legislature in enacting Section 40A(3) particularly was to ensure that payments exceeding the sum specified are made by a crossed cheque drawn on a bank or by a crossed bank draft so that it will be easier to ascertain, when deduction is claimed, whether the payment was genuine and whether it was made out of income from disclosed sources. While interpreting the provisions of this section, the above mischief which was sought to be remedied will have to be borne in mind."

It was further observed as follows :

".....The rigour of the rule contained in this sub-section is, however, relaxed to some extent by the second proviso to the said sub-section which provides that no disallowance under the said sub-section shall be made where any such payment is made otherwise than by a crossed cheque drawn on a bank or by a crossed bank draft, in such cases and under such circumstances may be prescribed, having regard to the nature and extent of banking facilities available, considerations of business expediency and other relevant factors. As pointed out by the Finance Minister in his speech in the Lok Sabha while introducing the Finance Bill of 1968, this proviso was introduced in order to obviate any difficulties in payment by cheques or bank drafts in rural areas and in certain other cases and circumstances. For that purpose, power was conferred to enact rules to prescribe cases and circumstances in which no disallowance under Sub-section (3) shall be made where any payment in a sum exceeding Rs. 2,500 is made otherwise than by a crossed cheque drawn on a bank or by a crossed bank draft."

7. With reference to the 3rd condition provided in the rule, viz., where payment in the manner provided in Section 40A(3) is not practicable the scope and ambit of the word "practicable" used in Rule 6DD(j)(2) was considered with reference to the dictionary meaning. It was observed that the word "practicable" must be held to signify that which is feasible, that is to say, capable of being put into practice, done, or accomplished with the available means and resources. It was also observed that in determining the practicability for the purposes of Rule 6DD(j)(2), regard will have to be had to the facts and circumstances of each case, for, in the ultimate analysis, it is the actuality which must be the decisive factor and that the taxing authority must approach a case which falls to be decided under Rule 6DD(j)(2) in the above light. It was further observed that the practicability for the purposes of Rule 6DD(j)(2) must be judged from the point of view of the businessman and not of the Revenue. Considering the above circumstances the Gujarat High Court observed as follows:

"We are, therefore, not prepared to unduly restrict the scope of Sub-clause (2) of Clause (j) of Rule 6DD by holding that in considering the practicability or otherwise of payment by a crossed cheque or a crossed bank draft, only the two circumstances enumerated therein can be taken into consideration. The correct interpretation, in our opinion, would be to give to the word "practicable" a wide

and liberal meaning as we have done above and to leave it to the ITO to judge in each case whether or not from the stand point of the business or professional man it was practicable to make payment by a crossed cheque or a crossed bank draft."

The Supreme Court in *Attar Singh Gurmukh Singh v. ITO*, (1991) 191 ITR 667 (SC) considered the constitutional validity of Section 40A(3) and Rule 6DD of the Rules. Repelling the challenge, the Supreme Court observed as follows :

"Section 40A(3) must not be read in isolation or to the exclusion of Rule 6DD. The section must be read along with the rule. If read together, it will be clear that the provisions are not intended to restrict the business activities. There is no restriction on the assessee in his trading activities. Section 40A(3) only empowers the AO to disallow the deduction claimed as expenditure in respect of which payment is not made by crossed cheque or crossed bank draft. The payment by crossed cheque or crossed bank draft is insisted on to enable the assessing authority to ascertain whether the payment was genuine or whether it was out of the income from undisclosed sources. The terms of Section 40A(3) are not absolute. Considerations of business expediency and other relevant factors are not excluded. Genuine and bona fide transactions are not taken out of the sweep of the section. It is open to the assessee to furnish to the satisfaction of the AO the circumstances under which the payment in the manner prescribed in Section 40A(3) was not practicable or would have caused genuine difficulty to the payee. It is also open to the assessee to identify the person who has received the cash payment. Rule 6DD provides that an assessee can be exempted from the requirement of payment by a crossed cheque or crossed bank draft in the circumstances specified under the rule. It will be clear from the provisions of Section 40A(3) and Rule 6DD that they are intended to regulate business transactions and to prevent the use of unaccounted money or reduce the chances to use black money for business transactions [See *Mudiam Oil Co. and Others Vs. Income Tax Officer and Others*, . If the payment is made by a crossed cheque drawn on a bank or a crossed bank draft, then it will be easier to ascertain, when deduction is claimed, whether the payment was genuine and whether it was out of the income from disclosed sources. In interpreting a taxing statute, the Court cannot be oblivious of the proliferation of black money which is under circulation in our country. Any restraint intended to curb the chances and opportunities to use or create black money should not be regarded as curtailing the freedom of trade or business."

8. As already noted, the only ground on which the AO had denied the claim for deduction of the transportation and coolie charges is that the assessee had not satisfactorily explained the circumstances under which the payments were made in cash. The Tribunal had considered the explanation of the assessee that the drivers of the vehicle in which raw cashewnuts were transported from Orissa to Kanyakumari District in Kerala State had insisted for payment of the transportation charges/coolie charges in cash and that they were not prepared to

receive crossed cheque or demand drafts and further that it is difficult to trace out those drivers for getting confirmatory letters in that regard. As per Circular No. 220, dt. 31st May, 1977, already referred, one of the special circumstances contemplated under Rule 6DD(j) is that the seller is refusing to accept the payment by way of crossed cheque/draft and the purchaser's business interest would suffer due to non-availability of goods otherwise than from this particular seller. The said circular also states that it would generally satisfy the requirements of Rule 6DD(j), if a letter to the above effect is produced in respect of each transaction falling within the categories listed above from the seller giving full particulars of his address, sales-tax number/permanent account number, if any, for the purposes of proper identification to enable the ITO to satisfy himself about the genuineness of the transaction.

9. In the instant case the Kerala Road Transport Company, who was the transporter had issued a certificate to the effect that they have received the transportation charges from the petitioner. It is also relevant to note here that the genuineness of the transport and the identity of the dealer had been established by the assessee. What remained was only the production of a confirmatory letter from the transporters regarding the fact that they insisted for the payment of the charges in cash. The Tribunal, we note, after adverting to the explanation of the assessee observed thus:

"If the truck drivers who were transporting raw nuts from Orissa to the assessee's factories in Kanyakumari District insisted on the payment in cash, that would definitely be exceptional or unavoidable circumstances to make the payment eligible for exclusion under Clause (i) of Rule 6DD(j). The genuineness of the payment has not been disputed by the Revenue authorities. The fact that the assessee had got the raw nuts transported in the trucks belonging to Kerala Road Transport Co. was also (not?) disputed. The learned representative of the assessee has explained the reason why the assessee could not get evidence or confirmation letters from the truck drivers to whom the payment was made. In exceptional and unavoidable circumstances, if the assessee had to make the payment in cash, we are of the view that such payments could not be disallowed u/s 40A(3)."

This is a presumption drawn by the Tribunal. No supporting material is produced.

10. Having regard to the object of introducing Section 40A(3) which was considered by the Gujarat High Court and by the Supreme Court and the interpretation placed by the Supreme Court and the Gujarat High Court on the provisions of Section 40A(3) r/w Rule 6DD(j) of the Rules we are of the view that one more opportunity has to be given to the assessee to produce confirmatory letters obtained from the transporting agency to the effect that they were not willing to receive the transportation charges by crossed cheque/draft and that they insisted for payment of the charges in cash. For the said purpose we set aside the order of the Tribunal and remit the matter to the Tribunal for fresh consideration after affording an opportunity to the parties and to pass fresh

orders in accordance with law in the light of the principles laid down by the Gujarat High Court and the Supreme Court in the decisions discussed above. In the circumstances we decline to answer the question referred.