(2014) 01 KL CK 0008

In the High Court Of Kerala

Case No : I.T.A. No. 87 of 2011

Commissioner of Income Tax	APPELLANT
Vs	
Muthoot General Finance	RESPONDENT

Date of Decision : 29-01-2014

Acts Referred:
Income Tax Act, 1961 — Section 31(1)(b), 37(1), 40(a)(ia), 40(b)(iv), 40A(3)

Citation : (2015) 370 ITR 543

Hon'ble Judges : Manjula Chellur, C.J;A.M. Shaffique, J

Bench : Division Bench

Advocate : P.K.R. Menon, Senior Counsel, Government of India (Taxes), and Jose Joseph, Standing Counsel, Advocates for the Appellant; T.M. Sreedharan, Senior Advocate, Nisha John, V.P. Narayanan and Boby M. Sekhar, Advocates for the Respondent

Judgement

Dr. Manjula Chellur, C.J.—The Revenue is before us in the above appeal. The appeal is admitted for consideration of the following substantial questions of law:

"1. Whether, on the facts and in the circumstances of the case and in the absence of any material produced to show that the purpose of drawing was to promote business and in view of the failure of the assessee to prove that the funds were given to partners on account of ''commercial expediency'', the Tribunal is right in law and fact in deleting the addition of Rs. 19,90,753 sustained by the Commissioner of Income-tax (Appeals)?

2. Whether, on the facts and in the circumstances of the case and also in view of the fact that the amount of Rs. 3.27 crores (Rs. 3,27,00,000) was not credited to the drawings account of Shri George Jacob and that the income disclosed in the return of income filed by Shri George Jacob is not correct--

(a) did not the Tribunal err in disallowing the interest of Rs. 3.27 crores paid to the partner, Shri George Jacob?

(b) did not the Tribunal err in disallowing the interest of Rs. 3,27,00,000 paid to the partner, Shri George Jacob?

3. Whether, on the facts and in the circumstances of the case, did not the Tribunal err in deleting the additions made under sections 40A(3) and 40(a)(ia)?

4. (a) Whether, on the facts and in the circumstances of the case and also for the reasons given by the Assessing Officer and the Commissioner of Income-tax (Appeals) read with ground G, the Tribunal is right in law and fact in deleting the addition of Rs. 12,18,00,000 (twelve crores eighteen lakhs) made under section 68 of the Income-tax Act?

(b) In the absence of detailed fund flow statement of the partner along with his balance-sheet and net wealth statement being produced, the Tribunal is right in law and fact in concluding that the partner utilised the funds withdrawn from the other two firms for depositing in the assessee''s firm and is not such a finding and conclusion perverse and based on surmises and conjectures?

5. Whether, on the facts and in the circumstances of the case and the concept of keyman insurance being as highlighted in ground I, the Tribunal is right in law and fact in deleting the premium of Rs. 61,29,162 on the ''keyman insurance policy''?

6. Whether, on the facts and in the circumstances of the case--

(a) are not the consideration of various disallowances and deletions by the Income-tax Appellate Tribunal by wrongly putting the burden of proof?

(b) should not the Income-tax Appellate Tribunal have put the assessee to proof?"

The facts that led to the present appeal in brief are as under. The assessee is a partnership concern engaged in the business of money lending and we are concerned with the assessment year 2006-07. Totally four additions made by the Assessing Officer became the subject matter of adjudication before the first appellate authority and the second appellate authority which are as under:

1. Interest chargeable on excess drawings effected by the partners of the firm amounting to Rs. 19,90,753.

2. Interest paid to one of the partners by name Sri George Jacob disallowed, i.e., Rs. 3,27,00,000.

3. Introduction of money by Mr. George Jacob, Rs. 12,18,00,000 one of the partners assessed, as income under other sources.

4. Premium of Rs. 61,29,162 paid towards keyman insurance which came to be disallowed by the Assessing Officer.

2. As a matter of fact the Assessing Officer in respect of the above four additions opined against the assessee which came to be challenged before the Commissioner of Income-tax (Appeals). Before the Commissioner of Income-tax (Appeals) all the four issues went against the assessee in favour of the Revenue.

This became the subject matter of challenge before the Income-tax Appellate Tribunal wherein the opinion of the first appellate authority came to be reversed so far as all the four issues answering against the Revenue. Therefore, Revenue is before us in this appeal seeking reversal of the order of the Appellate Tribunal.

3. So far as the excess drawings effected by the partners, according to the Assessing Officer, four partners by name Smt. Sara George, Smt. Susan Thomas, Smt. Elizabeth Jacob and Smt. Anna Alexander an amount of Rs. 166.30 crores was found during the course of assessment process. The Assessing Officer sought explanation from the firm why an interest at 12 per cent should not be charged on the excess drawings made by the partners. To which the assessee sent a reply on August 4, 2008, offering explanation saying as there was credit balance in the capital account of the partners during the financial year 2004-05, and since no interest was paid to them during the said financial year to their profit and loss account, hence interest chargeable on the current account as on March 31, 2006, was nil, they have not charged any interest on the over drawings. The said explanation was not accepted by the Assessing Officer for the reason that the assessee was in the habit of paying interest on the money borrowed by the firm and as a matter of fact the borrowed funds were diverted for the personal use of the partners, therefore, such expenditure incurred was not used for the business purpose. Hence, section 37(1) of the Income-tax Act has to be applied. He also opined that non-payment of interest to the partners in the previous financial year was irrelevant so far as not charging interest on the overdrawn amounts. Therefore, by calculating interest at 12 per cent per annum the Assessing Officer proceeded to disallow the said amount as interest. However, this came to be viewed from a different angle though Rs. 19,90,753 was made as additional income by the first appellate authority. The first appellate authority, while discussing the first issue, referred to partnership deed of the partners with regard to the provision for interest on excess drawings made by the partners. Though approved the opinion of the Assessing Officer in rejecting the explanation offered by the assessee, the Tribunal considered the matter in a more detailed manner. As the assessee-firm is dealing in money-lending business the specific rate of interest fixed under section 40(b)(iv) being 12 per cent the same rate of interest is payable by the firm on capital borrowings. It was difficult to believe that firm was not charging any interest on the amount drawn in excess by the partners. It also refers to the payment of Rs. 3.27 crores being interest to one of the partners, Sri George Jacob. From this, payment of interest was ascertainable, therefore, according to the first appellate authority, the Assessing Officer was justified in adding a sum of Rs. 19,90,753 being the interest on the excess drawn amounts by the partners. He also opined that the cash system of accounting does not provide any shelter to the explanation made by the assessee. General procedure followed by the professionals where cash system of accounting is followed is also indicated.

4. So far as this issue is concerned, he refers to the opinion of the Assessing Officer and also the first appellate authority in paragraphs 4, 5 and 6. Paragraph

7 refers to the arguments placed before the Tribunal with reference to paper book which was produced for the first time before the Tribunal by the assessee. At paragraph 8 of the order, the Tribunal opines that on going through the supporting documents filed, the addition cannot be sustained and further opines that the over drawings made by the partners should not have been charged with interest. In other words, it was compensated on account of non-payment of interest against the capital account of the partners in the previous year. The Tribunal also opines that so far as the group concern cash system of accounting supports their stand, therefore, interest can be taxed only when it is actually received. Hence, deleted addition of Rs. 19,90,753.

5. Then coming to the second issue, disallowance of interest paid to one of the partners, Mr. George Jacob, i.e., Rs. 3,27,00,000, the Assessing Officer opined that there is a debit to the profit and loss account of the assessee which indicates the total interest payment made by them and it amounts to Rs. 3,29,86,356. Out of this total amount of interest a huge chunk of interest amounting to Rs. 3.27 crores was paid to Mr. George Jacob, one of the partners. This was on the basis of credit balance appearing in the partner''s current account. But, however, interest was not seen credited to his drawing account. Further, interest receipt was not disclosed by the assessee in the return of income submitted by him for the assessment year 2006-07 before the Deputy Commissioner of Income-tax, Circle I, Thiruvalla. On account of this factual situation the claim of the assessee was rejected, therefore, this claim of payment of interest expenditure Rs. 3,27,00,000 was disallowed. In the profit and loss account for the year ending with March 31, 2006, this amount of Rs. 3,27,00,000 was not shown as income of Mr. George Jacob. So far as the expenditure and income pertaining to the present assessee, other details are given in the Commissioner of Income-tax (Appeals) orders.

6. So far as the second issue is concerned, the amounts actually shown as the capital amount of one of the partners, Sri George Jacob, were the amounts routed through other firms and, according to the appellate authority, this must have been done only to circumvent the provisions of section 40A(3), section 40(a)(ia), etc.; as all the entries for interest are only in cash entries and no payment reached through the bank. The entire money gone to the other firms only through the device of the partners'' account and, according to the appellate authority, it is all created for the purpose of avoiding the above provision. From this exercise undertaken by the assessee-firm, they draw two situations which could have been the intention of the assessee firm, i.e., though the partner has received Rs. 3.27 crores, he did not offer the same for tax and the second, partner has not factually received the money. According to the first appellate authority, it was only in the absence of non-compliance with the provisions of section 40A(3), etc., such conclusion alone is possible, therefore, affirms the opinion of the Assessing Officer in disallowing the interest expenditure. So far as this aspect of the matter, the Tribunal at paragraph 9 onwards discusses the same and opines that the term "expenditure" under section 40A(3) should not be

given an interpretation so as to adversely affect the assessee and, therefore, interest payment to the partners are not covered under section 40A(3). So far as section 40(a)(ia) he accepts the stand of the assessee and, according to the Tribunal, the interest has been offered by the partner in his individual return, therefore, there was no justification for the Assessing Officer to disallow the interest expenditure paid to this partner.

7. Then coming to the third issue, introduction of Rs. 12.18 crores by Sri George Jacob he refers to the explanation offered by the assessee to the query made by the Assessing Officer, how these amounts are reflected and the explanation was these amounts are amounts either received back or drawings effected from sister concern. The explanation was rejected by the Assessing Officer for want of proper explanation under section 68 of the Income-tax Act. So far as the opinion of the first appellate authority, he refers to the admission made by the assessee that Mr. George Jacob has admittedly introduced capital to the tune of Rs. 12.18 crores in the appellant firm and this amount was brought into account by cash shown as drawing from other firms. The respondent-assessee did not furnish any details with regard to the firm from where the said amounts were drawn, therefore, the Assessing Officer was justified in suspecting that genuineness of the transaction and creditworthiness of the said firm. According to the first appellate authority, though the stand of the appellant-assessee was that these amounts came to the hand of one of the partners or through other firms, i.e., Muthoot Bankers and Muthoot Properties but no balance-sheet pertaining to these two financial years were filed in support of the contention of the respondent-assessee. On the other hand, a perusal of the file pertaining to Muthoot Properties and Mar George Memorial Medical Centre, the appellant firm has drawn disallowance for investment in the appellant firm. Surprisingly this Rs. 12.18 crores did not find a place in the books of account of the appellant firm. The copy of the current account filed was rejected and was not taken into consideration. According to the first appellate authority, the respondent-assessee was under an obligation to establish how this Rs. 12.18 crores came to the account of the appellant firm as the facts were not matching with the stand of the assessee, therefore, the Assessing Officer was justified in opining the same as income of the appellant firm.

8. According to the Tribunal, on a perusal of records so far as one of the partners introducing Rs. 12.18 crores with the assessee-firm, the various sources of drawings made by him from the other firms like Muthoot Bankers and Muthoot Builders have been filed before the Assessing Officer, therefore, the assessee was able to establish the stand since the Assessing Officer did not attempt to verify such explanation of the assessee, he was not satisfied with the genuineness of the credit. It further opines, the Assessing Officer could have ascertained these facts by verifying the records pertaining to Muthoot Bankers and Muthoot Builders.

9. Then coming to the fourth issue with regard to the disallowance of premium

paid towards keyman insurance, the Assessing Officer opined that the keyman insurance policy means a life insurance policy taken by the person on the life of another person or for the employee of the person who took the policy or which was connected in any manner whatsoever with the business of the person who took the policy. Therefore, the policy being taken in the name of partners and in the absence of policies being taken either in the name of employees or any person engaged in any manner whatsoever with the business of the firm cannot be allowed as expenditure. The Assessing Officer also opines that since no material was forthcoming indicating that the benefit of the policy would ultimately go to the respondent-assessee, the expenditure towards payment of premium was disallowable. This opinion of the Assessing Officer was confirmed by the first appellate authority by referring to the judgment of the Mumbai Bench in the case of Modi Motors. Referring to section 40B the remuneration payable to the partners and also section 31(1)(b) the claim of the respondent-assessee was, there was no impediment to take the policy in the name of the partners of the firm, therefore, the opinion of the Assessing Officer and the first appellate authority was not justified. In other words, if the policy is taken in the name of a partner not for the personal benefit but for the benefit of the firm, it could be considered as expenditure to be allowed. Aggrieved by these findings of the Tribunal, the Revenue is before us.

10. What we notice from the orders of the first appellate authority and the Appellate Tribunal is that the first appellate authority as well as the Assessing Officer did not have the benefit of checking any of the records which were produced before the Tribunal as a paper book. Some of the documents which were part of the paper book produced before the Tribunal are placed before us as additional documents by filing an interlocutory application. Additional documents are, copies of account of four partners, copy of the common order in the case of Muthoot Bankers, Trivandrum in Income-tax Appellate Tribunal Cochin Bench, computation of income of Shri George Jacob and profit and loss account and balance-sheet of Shri George Jacob, true copy of the account of Shri George Jacob, true copy of the account of Shri George Jacob in Muthoot General Finance, true copy of the account of Shri George Jacob in Muthoot bankers and true copy of the account of Shri George Jacob in Muthoot Builders.

11. According to learned standing counsel for the appellant-Revenue, the additional documents now brought on record cannot be taken into consideration as they were not part of material produced before the Assessing Officer as well as the Commissioner of Income-tax (Appeals). According to him, this argument is based on the discussion made by the Assessing Officer and also the Commissioner of Income-tax (Appeals) especially with reference to the explanation given by the assessee to many queries with regard to the above four issues. He also brought to our notice certain discrepancies found in the additional documents contending that these documents do not reflect the correct and genuine picture supporting the stand of the respondent-assessee, therefore, no reliance could be placed on these documents.

12. It is noticed from the orders of the Assessing Officer, the Commissioner of Income-tax (Appeals) and the Tribunal that the entire system of accounting maintained by the respondent-assessee is by way of cash. It is also to be noted that similar accounting system is maintained so far as the sister firms and also the accounts of the partners including Mr. George Jacob. The stand of the respondent-assessee before both the appellate authorities was the funds coming to the respondent-assessee was belonging to one of the partners, i.e., Shri George Jacob and the funds reached him through other sister firms, therefore, there is proper explanation so far as Rs. 12.18 crores. So far as the non-payment of interest on excess amounts drawn by the partners of the firm they claim that certain capital amounts were available with the firm in respect of each of the four partners who had drawn excess amount, and as no interest was paid in the previous financial year, they did not charge any interest for the assessment year in question. Similarly, payment of Rs. 3.27 crores of interest to one of the partners is also inter-related to the other issue, i.e., whether Shri George Jacob, one of the partners, had brought Rs. 12.18 crores to the firm. So far as non-charging of interest on Rs. 19,90,753 lakhs overdrawn amount by a partner, the explanation offered by the respondent-assessee at the earliest opportunity before the Assessing Officer and the explanation now given also have to be taken into consideration. Now, the explanation is, no interest was paid in the previous year, therefore, they need not charge any interest. The first three issues are interconnected with each other which have to be dealt with reference to several accounts apart from the account of the respondent-assessee.

13. In order to arrive at a conclusion whether the four partners had excess amount in their account which attracted payment of interest, was there book adjustment of payment of interest has to be analysed with reference to the source of amounts brought in by those four persons to the respondent firm. Similarly, source for Rs. 12.18 crores as explained by the respondent-assessee has to be analysed with reference to the accounts of other sister concern firms and personal income-tax file of Mr. George Jacob.

14. In the light of the Tribunal placing reliance on paper book filed by the respondent-assessee in question which never was the subject matter of consideration before the Assessing Officer and the first appellate authority, we are unable to analyse the controversial issues raised before us with reference to the factual situation. Even otherwise, this court need not go into the veracity and genuineness of the facts placed on record now. In the light of absence of these additional documents for consideration before the Assessing Officer and the Commissioner of Income-tax (Appeals), one cannot conclude that the opinion of the Assessing Officer and the Commissioner of Income-tax (Appeals) were erroneous. Similarly, the Tribunal refers to several documents which persuaded reversal of the opinion of the Assessing Officer and the Commissioner of Income-tax (Appeals).

15. In the light of above factual situation, in the interest of justice the matter is

to be remanded back to the Assessing Officer, who has opportunity of seeking explanation and also the material available with the explanation of the assessee, to consider the entire matter afresh with reference to the documents filed in the form of paper book before the Tribunal. This exercise would bring to light whether the additional documents produced before the Tribunal were part of the records available before the Assessing Officer or not and it would also assist the Assessing Officer to appreciate the stand of the assessee. Thereafter, either accept the explanation or reject the same depending upon the facts and circumstances while considering the matter afresh on the merits. With these observations we set aside the orders of the Assessing Officer, the Commissioner of Income-tax (Appeals) and the Tribunal. The Assessing Officer is directed to proceed with the assessment proceedings afresh in the light of the above observations taking into consideration the paper book produced by the respondent-assessee before the Tribunal.

