
(2007) 05 AHC CK 0253
In the Allahabad High Court

Commissioner of Income Tax

APPELLANT

Vs

Raj Kumar Singh and Co.

RESPONDENT

Date of Decision : 15-05-2007

Acts Referred:

Income Tax Act, 1961 — Section 145, 256

Citation : (2007) 210 CTR 483 : (2007) 295 ITR 81

Hon'ble Judges : R.K. Agrawal, J;Bharati Sapru, J

Bench : Division Bench

Final Decision : Dismissed

Judgement

R.K. Agrawal, J.—The Tribunal, Allahabad has referred the following five questions of law u/s 256(1) of the IT Act, 1961 (hereinafter referred to as "the Act") for opinion to this Court:

1. Whether on the facts and in the circumstances of the case, the Tribunal was, in law, justified in holding that the assessee's claim for deduction of interest of Rs. 1,58,01,118 was allowable in full?
2. Whether on the facts and in the circumstances of the case, the Tribunal was, in law, justified in holding that in relation to the receipts from hiring of machineries, the provisions of Section 145(2) were not applicable and in directing the AO to accept the receipts shown by the assessee as correct?
3. Whether on the facts and in the circumstances of the case, the Tribunal was, in law, justified in taking into consideration the surplus of Rs. 12,87,58,000 arising out of amalgamation of shares as approved by the Hon'ble High Court, when it had not resulted in generation of any surplus cash funds and the increase in the capital was set off by corresponding increase in the value of assets which were not available for withdrawals by the partners and only the borrowings from depositors were available for withdrawals ?
4. Whether on the facts and in the circumstances of the case, the Tribunal was,

in law, justified in directing the AO to allow the entire expenditure on machinery repairs, when as per the terms of agreements the liability of such expenses was alleged by the Department to be on the hirer?

5. Whether on the facts and in the circumstances of the case, the Tribunal was, in law, justified in holding that depreciation and repairs were allowable in respect of 14 tippers and 1 tipper claimed to have been used as recovery van, when as per the details furnished by the assessee itself these machineries had not to be put to actual use and were only kept as a standby?

2. The reference relates to the asst. yr. 1990-91.

Briefly stated, the facts giving rise to the present reference are as follows:

The assessee is a partnership firm and is a sub-contractor of the firm M/s Jaiprakash Associates (for short "JPA") and has also certain dumpers and tippers etc., which it gives on hire to the contractors on daily basis. This firm has been running its business for the last several years. It had 91,970 shares, each valuing Rs. 100, in JPA in the asst. yr. 1986-87. On 31st Dec, 1985, JPA issued bonus shares in the ratio of 1 : 1 and, thus, the accumulation of the shares with the assessee firm amounted to 1,83,940. Investment in the original shares in the firm was Rs. 91,97,000. Thereafter, JPA was merged into J.P. Rewa Cement Public Ltd. Company (for short "JPR"). By the order of this Court, as per terms of agreement, 1 share of JPA was allotted 75 shares of JPR. In this way the total shares with the firm, on the basis of its holding of shares of JPA, amounted to Rs. 3,97,55,000 in JPR. These shares of JPR were of face value of Rs. 10 each. The firm showed its real value amounting to Rs. 13,97,55,000 in the accounts of the firm and after deducting initial investment of Rs. 91,97,000 from the said value, credited the balance amount of Rs. 12,87,58,000 in the respective shares of the partners in proportion to their shares and the abovesaid value was also adjusted in the accounts and the balance sheet of the firm. During the year, the partners withdrew Rs. 2,27,08,772 in total from the respective accounts. The assessee firm had also paid Rs. 1,58,01,118 as interest during the year to its depositors/creditors. The AO disallowed the said interest on the ground that the drawings by the partners were in excess of the deposits and thus, the interest paid on the borrowings was not for business purposes. In appeal, the learned CIT(A) also confirmed the said disallowance on the abovesaid plea and also on an additional ground that the interest paid to certain depositors/creditors who were directly related or friends of the partners of the assessee firm was also in excess of the reasonable interest. The CIT(A) held that the reasonable interest was of 20 per cent which is charged by the bank and, thus interest paid @ 24 per cent and 25 per cent to some of the creditors being in excess of that 20 per cent was also a point for the alleged disallowance. The assessee, being aggrieved, had come up in second appeal before the Tribunal. The Tribunal after hearing the parties at length on the point, decided the issue in paras 11 and 12 of its order, which runs as under:

11. We have heard the parties at length and we are of the opinion that the arguments advanced by the learned Counsel for the assessee have force and the Department appears to have gone on wrong premises and based the entire order on mere surmises and conjectures. The very fact that the assessee is not doing any other business except giving the tippers and dumpers on hire is not borne out from the fact. Admittedly the assessee firm is a sub-contractor and it has taken sub-contractors to the extent of crores of rupees and had been doing the said business for years. It may be possible that this year no other subcontractor might have been obtained by the assessee firm, yet it cannot be said that it has completely ceased to have any such business. From the details of the deposits and withdrawals during the year given out at p. 1 of the compilation, it is evident that the total borrowings amounted to Rs. 5,92,46,393 while the total payments to the creditors during the year amounted to Rs. 7,75,53,488. It means that the borrowings during the year were less than the payments made to the creditors. We fail to understand that under these circumstances how it can be said that the withdrawals were from the borrowings. In fact, the contention raised by the learned Counsel for the assessee has greater force that these borrowings were to repay the old borrowings. It has been pointed out that there was an advance of Rs. 5.74 crores (interest-free) from M/s Jaiprakash Associates (P) Ltd. during the asst. yr. 1986-87 and the said fact stands reflected from the balance sheet of the financial year 1985-86, which is alleged to have been filed in the compilation. It has further been pointed out that out of these advances, the assessee had made the following investments during the asst. yr. 1986-87 which are reflected in the balance sheet for the said year at Schedule "G--Investment attached to the balance sheet for the year ending 31st March, 1986 (copy filed in the compilation):

(a) Rs. 75,00,000 in 75,000 equity shares of Rs. 100 each in M/s Jaiprakash Associates (P) Ltd.

(b) Rs. 20,00,000 in 2,00,000 equity shares of Rs. 10 each of M/s J.P. Rewa Cement Ltd.

(c) Rs. 2,75,00,000 representing share application money invested in M/s J.P. Rewa Cement Ltd. for acquiring 27,50,000 equity shares.

(d) Rs. 22,500 in 2,250 equity shares of Rs. 10 each of J.P. Associates Construction Ltd.

Rs. 5,50,22,500 Total investment in shares.

12. It appears that it is to refund amounts that fresh deposits bearing interest were accepted during the year 1989-90 to the tune of Rs. 5,83,71,210 and out of the same, in the same assessment year i.e. 1989-90, Rs. 6,50,70,812 was paid back to M/s Jaiprakash Associates from whom the assessee firm had received excessive advance as reflected at p. 31 of the paper book. During the asst. yr. 1990-91, the deposits as mentioned above were less than the amounts paid. With all these details, we fail to understand as to how it can be said that the

deposits were not accepted for business purposes. When the assessee firm had invested the interest-free excessive advances received from Jaiprakash Associates in the asst. yr. 1986-87 itself, then if required to return the said amount, it had only two alternatives, either to sell its assets in the form of shares or to borrow money from the market on interest and pay the same. The company in its wisdom thought it proper to borrow the money from market and pay to Jaiprakash Associates instead of selling the shares and the said wisdom proved to be the real wisdom as the very shares increased in value far more than the interest paid by the firm. The very shares of Jaiprakash Associates of Rs. 100 was converted into 75 shares of JPR and the equity shares of JPR exceeded far in value in the asst. yr. 1990-91 as compared to its face value of Rs. 10. Over and above all this, the assessee received dividends during the year to the extent of more than Rs. 3 crores which was, in our opinion, far more than the interest paid by the assessee on its borrowings to which it had to resort for distress sale of its shares to repay the interest-free excessive advances received by the firm from Jaiprakash Associates. It has been more often that not held by the Hon''ble Supreme Court in its various decisions that the action/decision taken by a businessman has to be looked into with a view of the businessman and not with the view of a bureaucrat/taxing authority sitting in the office. We, therefore, feel that by no stretch of imagination it can be said that the borrowings were not for business purposes and once the borrowings were for business purposes, then the interest on the said borrowings had to be allowed under the law. Now, the only fact to be seen in this case is as to whether the withdrawals by the partners were justified or not. Whether the decision of the Hon''ble High Court, reported in the case of Commissioner of Income Tax Vs. H.R. Sugar Factory, and subsequently followed in the case reported at COMMISSIONER OF Income Tax Vs. SARAYA SUGAR MILLS (P.) LTD., applied to the present case or not. As far as these two decisions of Hon''ble Allahabad High Court are concerned, in our opinion, they do not have any application at all to the present facts of the case. In both those cases, there were excessive loans to the directors and at the same time borrowings by the company. Consequently, the interest was disallowed to the extent of the loans advanced to the directors without interest. Here in this case, the partners had not taken any loan from the firm. Firstly, they had withdrawn their amount from the credit entries standing in the name and secondly, the profits during the year and the deposits made by them (dividend warrants of the partners deposited with the firm) were far in excess than the withdrawals. The proposition laid down by the learned CIT(A) that the partners had absolutely no right to withdraw from the deposits with the firm has no legs to stand and cannot be accepted to be a correct proposition of law. The Hon''ble Gauhati High Court in the case of CIT v. Mehta Construction Co. (supra) has held that the withdrawals by the partners from their credits in the firm to purchase immovable property or to gift away to some of the relations was not improper unless specifically agreed upon in the partnership deed. Here in this case, the partnership deed has been filed in the compilation and there is no stipulation to the effect that the partners will not be permitted to withdraw the initial deposits made by them with the firm.

The Tribunal, in para 19, further gave its finding, which runs as under:

19. Taking the above circumstances into consideration, we hold that, firstly, there was no excess withdrawals by the partners during the year as the amounts deposits by them during the year (dividend + profits) was far in excess than the withdrawals. Secondly, the shares which were owned by the firm indirectly belonged to the partners and the amounts credited to their accounts in proportion to the shares was far in excess than the withdrawals. Thirdly, the interest paid on the borrowings was for business interest as the income borrowed during the year was far less than the amounts paid towards the old borrowings. On that score too, it cannot be said that the partners were advanced money out of the borrowings. In fact, we feel that this whole controversy has arisen in the minds of the taxing authorities by going through a wrong premise that the assessee had no other business except giving his dumpers and tippers on hire. In fact, the assessee was also a sub-contractor and had also invested money in the shares, which was permissible by the Partnership Act and any amount invested in the shares had paid huge dividends to the assessee which was far in excess than the interest liability of the assessee. In these circumstances, in our opinion, no interest was disallowable and the finding to the contrary by the learned CIT(A) is hereby cancelled and the issue is decided in favour of the assessee.

3. The assessee had dumpers and tippers and gave the same on hire to M/s Friends Construction and JPA. The total receipts disclosed were at Rs. 37,30,000 for the actual number of working days used. The AO applying the provisions of Section 145(2) estimated the receipts at Rs. 92,98,000 on the basis of 360 working days as per agreement in which it was mentioned that the hire charges would be received from the date of actual use. Besides, the slips prepared daily for the actual use could not be produced by the assessee on the ground that the same had outlived its utility as the same had been entered on a chart and the bills prepared and submitted to the hirers and there being no discrepancy in the bills raised and the amount received by the assessee firm. In absence of the primary evidence of those slips, the abovesaid estimate was made by the AO. In first appeal, the CIT(A) gave some relief and issued certain directions to reduce the number of working days. The assessee being aggrieved had gone in second appeal before the Tribunal. The Tribunal, after discussing the whole issue in detail, gave its finding in para 27 of its order, as under:

27. Taking the above discussion into consideration, we direct the AO should accept the receipts towards hire charges as the correct one and allow depreciation and repair charges, if any, on 14 dippers and one recovery van, which is alleged not to have been used during the year, while they were kept in readiness for use by the hirer at the site. The issue is decided accordingly.

4. The assessee had incurred an expenditure of Rs. 28,11,678 towards repairs and purchase of spares on its machinery. The said amount was disallowed on the ground that the receipts were too low and secondly the amount of repairs shown was too high in comparison to earlier year. The said disallowance was also

confirmed by the CIT(A). The assessee appealed to the Tribunal. The Tribunal gave its finding in para 33 deleting the said disallowance, as under:

33. Now the only point to be seen is as to how far the hirers were responsible for maintenance or repairs of the tippers and dumpers. A little careful scrutiny of the very agreement, copy of which is in the compilation, will show that the hirer were only responsible for minor repairs. The expenditure shown by the assessee is not on minor repairs but is of major repairs and on replacement of the spares of the machinery. It is also a hard fact that hirers are never responsible for major repairs unless specifically agreed upon in the agreement deed. Here, both the companies, M/s Friends Construction Co. and Jaiprakash Associates had only agreed in the agreement deed for minor repairs and not for major repairs. Hence the natural conclusion is that it has to be borne by the assessee firm and it was rightly borne by it. We, therefore, direct the AO to allow the entire expenditure meted out by the assessee firm on repairs and spares and its machinery. The issue is decided accordingly.

5. Regarding the disallowance of depreciation for repair expenses on 14 tippers and one recovery van on the ground that they were not used during the year for the purpose of business, the Tribunal, after hearing the parties, had allowed the depreciation and repair expenses of these tippers and delivery van on the ground that they were used by the hirer company constructively as they were kept in readiness for being used by the hirer at the site in case of any breakdown of the other dumpers and tippers or due to some emergency.

6. We have heard Sri R.K. Upadhaya, learned standing counsel for the Revenue. Nobody has appeared on behalf of the respondent assessee.

7. The first and third questions are interrelated. From the order of the Tribunal, we find that the respondent assessee had taken interest-free advance of Rs. 5.7 crores from the Jai Prakash Associates (P) Ltd. during the asst. yr. 1986-87. The said amount was required to be refunded/paid back for which there were two options available to the assessee, either to liquidate the assets or to borrow money from the market on payment of interest. The respondent assessee, as a prudent businessman, adopted the second option by borrowing the money from the market on payment of interest. It may be mentioned here that on the investment made by the respondent assessee, it has earned a dividend income of Rs. 3 crores, which, if utilised, would have liquidated the advance otherwise it would have resulted in loss of Rs. 3 crores. Thus, if as a prudent businessman, the assessee has decided to borrow money from the market, the interest paid is clearly allowable as a business expenditure.

8. Recently, the apex Court in the case of S.A. Builders Ltd. Vs. Commissioner of Income Tax (Appeals), Chandigarh and Another, , has held that the interest paid on expenditure incurred on account of commercial expediency, is allowable. The same principle would be applicable in the present case. Therefore, we are of the considered opinion that the claim of Rs. 1,58,01,118 regarding the interest was

allowable in full.

9. Question No. 3 is relatable to question No. 1. As there is no separate discussion in the statement of the case sent by the Tribunal, it is only an aspect of the availability of fund in the partners' capital account. In view of our answer to question No. 1, the question No. 3 really does not have any special significance.

10. So far as question No. 2 is concerned, we find that the Tribunal has recorded a clear finding of fact that the payment made by the hirer of the machineries, stood confirmed from the account books maintained by the hirer as also that of the assessee and no discrepancy of any major payment or payment not being recorded in the books of account, has been pointed out. If that is the situation, the provision of Section 145(2) of the Act was not attracted and the income has to be assessed on the basis of the actual receipt as disclosed by the assessee.

11. So far as question No. 4 is concerned, we find that under the terms of the agreement entered into between the assessee and the hirer, the responsibility of the hirer was only to effect minor repairs. It is not in dispute that the vehicles, namely, tippers and other vehicles, which were given on hire, had to be maintained by the assessee in case of major breakdown and failure. The expenditure incurred in respect of carrying out major repairs, was clearly to be met by the assessee and it was an allowable deduction.

12. So far as question No. 5 is concerned, under the agreement, the assessee was required to provide 14 tippers and one tipper recovery van as standby so that in the event of any major breakdown or otherwise if the vehicles on hire were not capable of being used, extra tipper provided as standby could have been used. The depreciation and repairs were clearly admissible on such vehicles which were provided as stand by.

13. In view of the foregoing discussions, we answer all the questions referred to us in favour of the assessee and against the Revenue. There shall be no order as to costs.