(1991) 04 AHC CK 0096

In the Allahabad High Court

Case No : Income-tax Reference No. 1014 of 1978

Commissioner of Income Tax APPELLANT

Vs

Raja Ram Jaiswal RESPONDENT

Date of Decision : 04-04-1991

Acts Referred:
Income Tax Act, 1961 — Section 256(2)

Citation : (1992) 195 ITR 834

Hon'ble Judges : B.P. Jeevan Reddy, C.J;S.R. Singh, J

Bench : Division Bench

Final Decision : Dismissed

Judgement

B.P. Jeevan Reddy, C.J.—u/s 256(2) of the Income Tax Act, 1961, the Tribunal stated the following two questions :

"(1) Whether, on the facts and in the circumstances of the case, the payments in question constituted in law application of income or diversion of income at source by on overriding title ?

(2) Whether, on the facts and in the circumstances of the case, the payments in question constituted expenditure on capital account or was it a revenue expenditure ?"

The assessee is an individual. The assessment year concerned herein is 1970-71. During the assessment proceedings, the assessee raised a claim before the Income Tax Officer that he had borrowed certain amounts from two persons, namely, Sarvsri Mahabir Lal and Hira Lal, which amount he invested in a firm, Messrs. Raja Ram Jamuna Prasad Banarsi Lal Shambhoo Nath, in which firm the assessee had a share to the extent of 60%. The petitioner''s case was that he entered into an agreement with the aforesaid two lenders some time in the year 1969, whereunder he had agreed to pay the said two persons 7% and 13% out of the share income received by him from the said firm. He, accordingly, claimed that the amount representing 20% should not be treated as his income since that income is being diverted to the said lenders under an overriding title. According to him, it was not a case of application of income at all. This plea was, however, rejected by the Income Tax Officer whereupon the assessee carried the matter in appeal which was dismissed. The assessee then carried the matter in further appeal to the Tribunal. The Tribunal agreed with the assessee that it was a case of diversion by virtue of an overriding title. Thereupon, the Revenue obtained this reference.

2. It may be noticed that the said agreements between the assessee and the said lenders were practically in the nature of a sub-partnership. It was not a case where the assessee could at any time pay up the loans and discharge/terminate the agreements. Evidently, the said lenders were prepared to lend the amount only on the condition that they were given a share in the share interest of the assessee. The amount thus payable to the said lenders cannot be said to have come into the hands of the assessee and applied by him towards the payment of interest or other liabilities. It was a case where the said lenders were deriving the said income on the basis and by virtue of their own title and interest, created no doubt by the agreements aforesaid. It has been held that an amount diverted by virtue of a partnership agreement or sub-partnership agreement is tantamount to diversion by overriding title. While it is not necessary to refer to all the decisions in this behalf, it would be sufficient if we refer to the decision of the Madras High Court in Commissioner of Income Tax Vs. S. Arumugham Pillai, . The assessee in that case was a partner in a firm ''S'' He was also a partner in firm ''J''. ''J'' had advanced money to ''S'' as and when required. The amount of advance was treated in the books of ''S'' as the capital of the assessee. Under a written agreement between the assessee and the other two partners of ''J'', it was agreed that the income of the assessee from ''S'' as partner was to be shared by the assessee and the said two other partners of ''J''. The question was whether the amount paid to the said two other partners of ''J'' was a case of application of income by the assessee or a case of diversion of income by overriding title. It was held that it fell in the latter category. To the same effect is the decision of the Delhi High Court in L. Hans Raj Gupta and Another Vs. The Commissioner of Income Tax, . The principle, of course, is set out in the decision of the Supreme Court in Fatehchand Murlidhar and Another Vs. Commissioner of Income Tax, Calcutta, .

3. For the above reasons, question No. 1 is answered in the following words :

"The payments in question constitute a case of diversion of income at source by an overriding title."

So far as question No. 2 is concerned, it need not be answered in view of our answer to question No. 1.

4. Reference is answered accordingly. No order as to costs.

