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**(1993) 08 BOM CK 0051**

**In the Bombay High Court**

**Case No : Income-tax Reference No. 117 of 1980**

Phaltan Sugar Works Ltd.

APPELLANT

Vs

Commissioner of Wealth-tax.

RESPONDENT

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**Date of Decision : 27-08-1993**

**Acts Referred:**

Income Tax Act, 1961 — Section 36(1), 40A(5)

**Citation : (1994) 208 ITR 989**

**Hon'ble Judges : D.R. Dhanuka, J;B.P. Saraf, J**

**Bench : Division Bench**

**Advocate : Dilip Dwarkadas, for the Appellant; G.S. Jetley, for the Respondent**

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## **Judgement**

D.R. Dhanuka J.

1. The Income Tax Appellate Tribunal, Bombay Bench, "E", Bombay, has referred the following questions to this court for its opinion u/s 256(1) of the Income Tax Act, 1961 :

2. At the instance of the Revenue :

"1. Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding the interest on loans borrowed for advancing if to its subsidiary company was allowable u/s 36(1)(iii) of the Income Tax Act, 1961 ?

2. Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that reimbursement of medical expenses were part of salary and not perquisites for the purpose of disallowance u/s 40A(5) of the Income Tax Act, 1961 ?"

3. At the instance of the assessee :

"1. Whether, on the facts and in the circumstances of the case, the Tribunal was justified in not allowing the assessee's claim for a sum of Rs. 29,83,126 ?

2. Whether, on the facts and in the circumstances of the case, the Tribunal was

right in directing the Income Tax Officer to treat the reimbursement of medical expenses as part of salary paid to the directors of the assessee-company ?

3. Whether on the facts and in the circumstances of the case, the interest of Rs. 3,87,765 was a permissible deduction as a revenue expenditure ?

4. Whether, on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was right in holding that no appeal lies against the levy of interest by the Income Tax Officer u/s 215 of the Income Tax Act, 1961 ?"

4. It is agreed between counsel that question No. 2 referred to this court at the instance of the Revenue is covered by the decision of this court in the case of Commissioner of Income Tax, Bombay City-III, Bombay Vs. Mercantile Bank Ltd., in favour of the assessee.

5. It is agreed between counsel that question No. 1 referred at the instance of the assessee is covered by the judgment of this court dated March 22, 1993, in Income Tax Reference No. 356 of 1980, in the case of Ravalgaon Sugar Farm Ltd. v. CIT [1994] 208 ITR 994. Following the ratio of the said decision, we answer the said question in the negative and in favour of the assessee.

6. It is agreed between counsel that question No. 2 referred at the instance of the assessee is also covered by the decision of this court in the case of Commissioner of Income Tax, Bombay City-III, Bombay Vs. Mercantile Bank Ltd., . Following the ratio of the said decision, we answer the said question in the negative and in favour of the assessee.

7. It is agreed between counsel that question No. 3 referred at the instance of the assessee is covered by the ratio of the judgment of this court in the case of Commissioner of Income Tax, Bombay City-III Vs. Shree Changdeo Sugar Mills Ltd., . Following the ratio of the said decisions, we answer the said question in the negative and in favour of the Revenue.

8. It is agreed between learned counsel that questions No. 4 referred at the instance of the assessee is covered by the judgment of the Supreme Court in the case of Central Provinces Manganese Ore Co. Ltd. Vs. Commissioner of Income Tax, . Following the ratio of the said judgment, we answer the said question in the affirmative and in favour of the Revenue.

9. Learned counsel on both sides concentrated on question No. 1 referred at the instance of the Department. Both learned counsel urged their respective contentions on this question only.

10. The relevant facts having a bearing on the said questions are briefly summarised as under :

(a) This reference concerns assessment year 1973-74. During the assessment year, the assessee borrowed loans from the UCO Bank and the UW Bank Ltd. The assessee paid interest on the said borrowings to the banks concerned. The assessee, however, did not utilise substantial part of the said loan for its own

business. Messrs. Haverro Industries Ltd. is a 100 per cent. subsidiary of the assessee. The assessee passed on the amount of loan in question to the said subsidiary company for the business of the subsidiary company. During the assessment year, the subsidiary company made a profit of Rs. 13,57,900. The assessee did not charge any interest to the said subsidiary company on the amount of loan in question. The assessee used to charge interest to the subsidiary company in the previous year. After taking an overall view of the facts and circumstances of the case, the Income Tax Officer reached the conclusion that the amount of interest paid by the assessee to the banks concerned could not be allowed as deductible expenditure in respect of loans utilised by the subsidiary company for its own business. The Income Tax Officer thus disallowed the claim of the assessee for deduction of the interest paid to the banks concerned in so far as the said claim pertained to money utilised by the above referred subsidiary company. It is not disputed that the subsidiary company is a separate legal entity and the business of the subsidiary company cannot be considered as the business of the assessee itself. Thus, the interest on money borrowed by the assessee for the purpose of business of the subsidiary company could not be deductible from the income of the assessee u/s 36(1)(iii) of the Act.

(b) Being aggrieved by the said order passed by the Income Tax Officer, the assessee preferred an appeal before the Appellate Assistant Commissioner of Income Tax. The Appellate Assistant Commissioner upheld the disallowance of the interest made by the Income Tax Officer concerning the amount of bank loans utilised by Messrs. Haverro Industries Limited for its business. The assessee did not even charge interest to the subsidiary company for the monies utilised by the subsidiary company on the ground that the financial condition of the subsidiary company had been going from bad to worse as on March 31, 1976. The assessee passed a board resolution to the effect that the interest be waived by the assessee-company on the ground of commercial expediency. The Income Tax Appellate Tribunal reversed the orders passed by the Appellate Assistant Commissioner on this subject. The Tribunal held that the assessee was entitled to deduction in respect of the interest on the amounts borrowed and utilised by the subsidiary company as the amounts in question can be said to have been borrowed by the assessee-company for the purpose of its own business.

11. Section 36(1)(iii) of the Income Tax Act, 1961, provides for deduction for payment of interest only if the assessee borrows capital for its own business. The business of the subsidiary company cannot be considered in law as the business of the assessee. The finding of the Tribunal based on commercial expediency appears to us to be incorrect. The fact remains that the money borrowed were utilised for business of the subsidiary company and not for the business of the assessee as such. In this view of the matter, we hold that the Tribunal was not justified in holding that the interest on loans borrowed for advancing to its subsidiary company was allowable u/s 36(1)(iii) of the Income Tax Act, 1961. The plain language of section 36(1)(iii) of the Income Tax Act, 1961, militates against the submissions urged on behalf of the assessee.

12. In view of the discussion, we answer question No. 1 referred to us at the instance of the Revenue in the negative and in favour of the Revenue.

13. Having regard to the facts and circumstances of the case, there shall be no order as to costs.

14. Issue of certified copy is expedited.