Commissioner of Income-Tax, West Bengal-III, Calcutta

Vs

Rajendra Prasad Moody, Calcutta and Others (tax reference case no. 1 of 1971) and Commissioner of Income-Tax, West Bengal-III, Calcutta

Vs

Raghunandan Prasad Moody, Calcutta. (Tax Reference Case No. 2 of 1971).

Tax Reference Case Nos. 1 and 2 of 1971

(P. N. Bhagwati, V. D. Tu;zapurkar, R. S. Pathak JJ)

04.10.1978

JUDGMENT

BHAGWATI, J. -

1.These are two references made by the Tribunal to this Court under Section 257 of the Income Tax Act, 1961 in view of a conflict in the decisions of High Courts on the question as to whether interest on monies borrowed for investment in shares is allowable expenditure under Section 57(iii) when the shares have not yielded any return in the shape of dividend during the relevant assessment year. The preponderance of judicial opinion is an favour of the view that such interest is admissible, even though no dividend is received on the shares, but there are two High Courts which have taken a different view and hence it is necessary for this Court to set the controversy at rest by finally deciding the question. Since the question is purely one of law turning on the true interpretation of Section 57(iii), it is not necessary to set out the facts giving rise to these two references in any detail. It would be sufficient to state that the assessee in these two reference are brothers and each of them had borrowed monies for the purpose of making investment in shares of certain companies and during the assessment year 1965-66 for which the relevant accounting year ended on April 10, 1965, each of the two assessees paid interest on the monies borrowed but did not receive any dividend on the shares purchased with those monies. Each of the two assessees made a claim for deduction of the amount of interest paid on the borrowed monies but this claim was negatived by the Income Tax Officer and on appeal by the Appellate Assistant Commissioner on the ground that during the relevant assessment year the shares did not yield any dividend and, therefore, interest paid on the borrowed monies could not be regarded as expenditure laid out or expended wholly and exclusively for the purpose of making or earning income chargeable under the Head "Income From Other Sources" so as to be allowable as a permissible deduction under Section 57(iii). The Tribunal, however, on further appeal, disagreed with the view taken by the taxing authorities and upheld the claim of each of the two assessees for deduction under Section 57(iii). The Revenue being aggrieved by the decision of the Tribunal made an application in each case of reference of the following question of law, namely :

> Whether on the facts, and in the circumstances of the case, interest on money borrowed for investment in shares which had not yielded any dividend is admissible under Section 57(iii) ?

> and since there was divergence of judicial opinion on this question, the Tribunal referred it directly for the opinion of this Court.

2. The determination of the question before us turns on the true interpretation of Section 57(iii) and it would, therefore, be convenient to refer to that section, but before we do so, we may point out that Section 57(iii) occurs in a fasciculus of sections under the heading 'F-Income From Other Sources'. Section 56 which is the first in this group of sections enacts in sub-section (1) that income of every kind which is not chargeable to tax under any of the heads specified in Section 14, Items A to E, shall be chargeable to tax under the head 'Income From Other Sources' and sub-section (2) includes in such income various items, one of which is 'dividends'. Dividend on shares is thus income chargeable under the head 'Income From Other Sources'. Section 57 provides for certain deductions to be made in computing the income chargeable under the head "Income From Other Sources" and one of such deductions is that set out in clause (iii) which reads as follows :

> Any other expenditure (not being in the nature of capital expenditure) laid down or expended wholly and exclusively for the purpose of making or earning such income.

The expenditure to be deductible under Section 57(iii) must be laid out or expended wholly and exclusively for the purpose of making or earning such income. The argument of the Revenue was that unless the expenditure sought to be deducted resulted in the making or earning of income, it could not be said to be laid out or expended for the purpose of making or earning such income. The making or earning of income, said the Revenue, was a sine qua non to the admissibility of the expenditure under Section 57(iii) and, therefore, if in a particular assessment year there was no income, the expenditure would not be deductible under that section. The Revenue relied strongly on the language of Section 37(1) and contrasting the phraseology employed in Section 57(iii) with that in Section 37(1), pointed out that the Legislature had deliberately used words of narrower import in granting the deduction under Section 57(iii), Section 37(1) provided for deduction of expenditure laid out or expended wholly and exclusively for the purpose of the business or profession in computing the income chargeable under the head 'Profits or gains of business or professions'. The language used in Section 37(1) was "laid out or expended .... for the purpose of the business or profession" and not "laid out or expended .... for the purpose of making or earning such income" as per out in Section 57(iii). The words in Section 57(iii) being narrower, contended the Revenue, they cannot be given the same wide meaning as the words in Section 37(1) and hence no deduction of expenditure could be claimed under Section 57(iii) unless it was productive of income in the assessment year in question. This contention of the Revenue undoubtedly found favour with the High Court but we do not think we can accept it. Our reasons for saying so are as follows.

3. What Section 57(iii) requires is that the expenditure must be laid out or expended wholly and exclusively for the purpose of making or earning income. It is the purpose of the expenditure that is relevant in determining the applicability of Section 57(iii) and that purpose must be making or earning of income. Section 57(iii) does not require that this purpose must be fulfilled in order to qualify the expenditure for deduction. It does not say that the expenditure shall be deductible only if any income is made or earned. There is in fact nothing in the language of Section 57(iii) to suggest that the purpose for which the expenditure is made should fructify into any benefit by way of return in the shape of income. The plain natural construction of the language of Section 57(iii) irresistibly leads to the conclusion that to bring a case within the section, it is not necessary that any income should in fact have been earned as a result of the expenditure. It may be pointed out that an identical view was taken by this Court in Eastern Investments Ltd. v. Commissioner of Income-tax (1951 SCR 594 : (1951) 20 ITR 1 : AIR 1951 SC 278), where interpreting the corresponding provision in

Section 12(2) of the Income Tax Act, 1922 which was ipsissima verba in the same terms as Section 57(iii), Bose, J., speaking on behalf of the Court observed : "It is not necessary to show that the expenditure was a profitable one or that in fact any profit was earned". It is indeed difficult to see how, after this observation of the Court, there can be any scope for controversy in regard to the interpretation of Section 57(iii).

4. It is also interesting to note that, according to the Revenue, the expenditure would disqualify for deduction only if no income results from such expenditure in a particular assessment year, but if there is some income, howsoever small or meagre, the expenditure would be eligible for deduction. This means that in a case where the expenditure is Rs. 1000, if there is income of even Re. 1, the expenditure would be deductible and there would be resulting loss of Rs. 999 under the head 'Income From Other Sources'. But if there is no income, then, on the argument of the Revenue, the expenditure would have to be ignored as it would not be liable to be deducted. This would indeed be a strange and highly anomalous result and it is difficult to believe that the Legislature could have ever intended to produce such illogicality. Moreover, it must be remembered that when a profit and loss account is cast in respect of any source of income, what is allowed by the statute as proper expenditure would be debited as an outgoing and income would be credited as a receipt and the resulting income or loss would be determined. It would make no difference to this process whether the expenditure is X or Y or nil; whatever is the proper expenditure allowed by the statute would be debited. Equally, it would make no difference whether there is any income and if so, what, since whatever it be, X or Y or nil, would be credited. And the ultimate income or loss would be found. We fail to appreciate how expenditure which is otherwise a proper expenditure can cease to be such merely because there is no receipt of income. Whatever is a proper outgoing by way of expenditure must be debited irrespective of whether there is receipt of income or not. That is the plain requirement of proper accounting and the interpretation of Section 57(iii) cannot be different. The deduction of the expenditure cannot, in the circumstances, be held to be conditional upon the making or earning of the income.

5. It is true that the language of Section 37(1) is a little wider than that of Section 57(iii), but we do not see how that can make any difference in the true interpretation of Section 57(iii). The language of Section 57(iii) is clear and unambiguous and it has to be construed according to its plain natural meaning and merely because a slightly wider phraseology is employed in another section which may take in something more, it does not mean that Section 57(iii) should be given a narrow and constricted meaning not warranted by the language of the section and in fact, contrary to such language.

6. This view which we are taking is clearly supported by the observations of Lord Thankenton in Hughes v. Bank of New Zealand (1938) 6 ITR 636 (House of Lords) where the learned Law Lord said :

> Expenditure in the course of the trade which is unremunerative is none the less a proper deduction, if wholly and exclusively made for the purposes of the trade. It does not require the presence of a receipt on the credit side to justify the deduction of an expense.

We find that the same view has been taken by the Madras High Court in K. Appa Rao v. Commissioner of Income-tax (1962) 46 ITR 511 (Mad HC), and P. V. Mohammed Ghouse v. Commissioner of Income-tax (1963) 49 ITR 127 (Mad HC), the Bombay High Court in Ormerods (India) Private Ltd. v. Commissioner of Income-tax (1959) 36 ITR 329 (Bom HC), the Allahabad

High Court in Chhail Behari Lal v. Commissioner of Income-tax (1960) 39 ITR 696 (All HC), the Madhya Pradesh High Court in Commissioner of Income-tax v. Dr. Fida Hussain G. Abbasi (1969) 71 ITR 314 (MP HC), the Kerala High Court in M. N. Ramaswamy Iyer v. Commissioner of Income-tax (1969) 71 ITR 218 (Ker HC) and the Orissa High Court in Commissioner of Income-tax v. Gopal Chand Patnaik (1977) 111 ITR 86 : 1976 Tax LR 443 (Ori HC). This view is eminently correct as it is not only justified by the language of Section 57(iii) but it also accords with the principles of commercial accounting. The contrary view taken by the Patna High Court in Maharajadhiraj Sir Kameshwar Singh v. Commissioner of Income-tax (1957) 32 ITR 377 (Pat HC) and the Calcutta High Court in Madanlal Sohanlal v. Commissioner of Income-tax (1963) 47 ITR 1 (Cal HC) must in the circumstances be held to be incorrect.

7. We accordingly answer the question referred to us for our opinion in each of these two references in favour of the assessee and against the Revenue. The Revenue will pay the costs of both the references to the assessee.

</html