East India Pharmaceutical Works Ltd.

Vs

Commissioner of Income-Tax.

Civil Appeal No. 1803 of 1981

(S. C. Agarwal, G. B. Pattanaik JJ)

11.03.1997

JUDGMENT

G.B. PATTANAIK J. –

1. This appeal by grant of certificate under section 261 of the Income-tax Act, 1961 (hereinafter referred to as the Act), by the High Court of Calcutta is directed against the judgment and order of the Calcutta High Court (see [1978] 114 ITR 591), dated April 21, 1978, in Income-tax Reference No. 404 of 1975. On an application being filed before the Income-tax Appellate Tribunal under section 256(1) of the Act the Tribunal referred the following question for being answered by the High Court (at page 593) :

> "Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that the payment of interest of Rs. 28,488 on money borrowed for payment of income-tax was not an expenditure laid out wholly and exclusively for the purpose of business as contemplated by sub-section (1) of section 37 of the Income-tax Act, 1961 ?"

The assessee is a company having an overdraft account with a bank. During the assessment year 1972-73, the assessee claimed a sum of rupees 28,488 as an allowable expenditure under section 37(1) of the Act, the said amount representing the interest which the assessee had to pay on the overdraft amount, the said overdraft having been made for the payment of income-tax. The Income-tax Officer disallowed the aforesaid deduction claimed by the assessee as he was of the opinion that the payment of income-tax cannot be held to be payment for the purpose of business. Being aggrieved by the said order, the assessee preferred an appeal and the appellate authority agreeing with the Assessing Officer came to hold that the overdraft utilised for payment of tax cannot be said to be for the business purposes of the company. In coming to the aforesaid conclusion the appellate authority relied upon the decision of the Calcutta High Court in the case of Mannalal Ratanlal v. CIT [1965] 58 ITR 84. The assessee then carried the matter in second appeal before the Tribunal. Before the Tribunal it was contended by the assessee that the tax liability being to the tune of a couple of lakhs, if the said liability would not have been discharged, then the entire business of the assessee would have been crippled and, therefore, discharge of such liability from the overdraft account would be held to be an expense for business purpose. The Tribunal, however, relying upon the decisions of the Calcutta High Court in Mannalal Ratanlal v. CIT [1965] 58 ITR 84 and CIT v. Calcutta Landing and Shipping Co. Ltd. [1970] 77 ITR 575, came to hold that me interest on money borrowed for payment of tax cannot be considered to be an allowable deduction in computing business profits. Having dismissed the assessee's second appeal, the Tribunal on an application being made referred the question for being answered by the High Court, as already stated. The High

Court of Calcutta by the impugned judgment came to the conclusion that an expenditure cannot be allowed as a business expenditure under section 37(1) of the Act, Unless it was incurred or laid out directly or indirectly by an assessee wholly and exclusively for the purpose of his business. It also came to the conclusion that the payment of income-tax will not fall within the scope of the expression "for the purpose of business". Relying upon the judgment of this court in CIT v. Birla Cotton Spinning and Weaving Mills Ltd. [1971] 82 ITR 166, it came to hold that the amount paid as income-tax is not an expenditure, not even a business expenditure and, therefore, the interest paid by a trader on the money borrowed for the payment of income-tax cannot be held to be a business expenditure on any commercial principle, not even on the ground of commercial expediency. It also further held that the payment of income-tax on the interest on the borrowed money for the payment of income-tax is not at all related with the purpose and object of the business and no element of trade in its commercial sense is involved in it. With this conclusion the High Court answered the question posed in the affirmative and in favour of the Revenue and against the assessee and thus this appeal.

Mr. Deepak Bhattacharya, learned counsel appearing for the appellant, argued with vehemence that the assessee having deposited the entire profits in the overdraft account and the amount thus deposited in the overdraft account being much more compared to the income-tax liability and the tax paid, it should have been presumed that in essence and true character the taxes were paid out of the profits of the relevant year and not out of the overdraft account for the running of the business. Consequently, the interest paid by the assessee on the overdraft account relatable to the payment of income-tax should have been allowed as an admissible deduction in the computation of the assessee's business income. In support of this contention, learned counsel appearing for the appellant relied upon the decisions of the Calcutta High Court in Woolcombers of India Ltd. v. CIT [1982] 134 ITR 219, Reckitt and Colman of India Ltd. v. CIT [1982] 135 ITR 698. Indian Explosives Ltd. v. CIT [1984] 147 ITR 392, and Alkali and Chemical Corporation of India Ltd. v. CIT [1986] 161 ITR 820. Learned counsel also urged that these decisions having been allowed to be operative for more than 14 years, the principle of stare decisis should be made applicable and, therefore, it must be held that the High Court committed an error in not accepting the assessee's contention. Learned counsel also placed before us a schedule appended to the assessment order to indicate that the amount of receipts deposited in the overdraft account was much more compared to the tax paid, for the purpose of raising the presumption that the said payment was out of the profit, in the light of the observations made by the Calcutta High Court in the four decisions referred to supra. Learned counsel appearing for the Revenue, on the other hand, contended that this contention as raised by counsel for the assessee had in fact not been raised either before the High Court or before the Tribunal and, as such this question never arose out of the order of the Tribunal. According to learned counsel for the Revenue, the question referred by the Tribunal to the High Court under section 256(1) of the Act was merely relatable to an interpretation of section 37(1) of the Act and whether the interest paid on the money borrowed for payment of income- tax can be held to be an expenditure allowable in computing the income under section 37(1) of the Act. Learned counsel further urged that in view of the decision of this court in the case of Madhav Prasad Jatia v. CIT [1979] 118 ITR 200 as well as the decision of this court in the case of Smt. Padmavati Jaikrishna v. Addl. CIT [1987] 166 ITR 176, no deduction can be claimed by an assessee in respect of the interest on borrowed capital made for discharge of the income-tax liability. According to learned counsel, the liability for payment of income-tax is a personal one and payment thereof is not to earn income but to meet the statutory liability and, therefore, the expenditure thus incurred cannot be held to be wholly and exclusively for the purpose of earning income within the ambit of section 57(iii) of the Act.

Having considered the rival submissions at the Bar, though we find considerable force in the arguments advanced by learned counsel appearing for the appellant, but in the facts and circumstances of the present case, on going through the order of the Tribunal as well as the question referred by the Tribunal for being answered by the High Court and the arguments advanced before the Tribunal as well as in the High Court by counsel appearing for the assessee, it is not possible for us to hold that any such contention, as was advanced before thus court by the assessee had in fact been advanced either before the Tribunal or before the High Court. The question whether a presumption can be drawn that the taxes were paid out of the profits of the relevant year and not out of the overdraft account for the running of the business as was drawn in Woolcomber's case [1982] 134 ITR 219 by the Calcutta High Court and was followed in three other cases of the same High Court, would essentially depend upon the fact as to whether the entire profits had been pumped into the overdraft account, whether such profits were more than the tax amount paid for the relevant year and all other germane factors. But when the assessee never advanced the contention either before the Tribunal or before the High Court and the amplitude of the question posed before the High Court does not bring within its sweep the contention as is advanced by Mr. Bhattacharyya, learned counsel in this court, it would not be appropriate for this court to look into the additional papers produced by the assessee for entertaining the contention and answering the same. It is true that the Calcutta High Court in Woolcombers' case [1982] 134 ITR 219 came to the conclusion that where profits were sufficient to meet the advance tax liability and profits were deposited into the overdraft account of the assessee, then it should be presumed that the taxes were paid out of the profits of the year and not out of the overdraft account for the running of the business. But to raise the presumption in that particular case there were sufficient materials and the assessee had urged the contention before the High Court. The aforesaid decision has been followed in the case of Reckitt [1982] 135 ITR 698, where without any further discussion Woolcombers' case [1982] 134 ITR 219 (Cal), has been followed. But it may be noticed that the question posed in Reckitt's case [1982] 135 ITR 698 was directly to the effect as to where the entire trading receipts were deposited by the assessee in the overdraft account and the tax was paid out of the overdraft account, whether the interest paid by the assessee for payment of tax out of the overdraft account is an allowable deduction. In Indian Explosives Ltd.'s case [1984] 147 ITR 392 (Cal), the aforesaid two decisions of the Calcutta High Court had been followed and the question that had been posed was to the effect whether the interest on an overdraft account paid towards the amount drawn for discharging the tax liability could be an allowable expenditure and, therefore, the High Court answered it in favour of the assessee and against the Revenue. It may be noticed that in the aforesaid case the court did not express any opinion on the question whether the interest paid on money borrowed for payment of tax was allowable as business expenditure. To the same effect is the decision of the Calcutta High Court in Alkali and Chemical Corporation of India Ltd. [1986] 161 ITR 820. It may be noticed that in the present case even before the Tribunal what was argued on behalf of the assessee is that the amount of interest paid to the bank represents an expenditure laid out or expended wholly and exclusively for the purpose of business. In furtherance of this contention it has also been urged before the Tribunal that non-payment of the taxes which were to the tune of lakhs would have entirely crippled the business of the assessee and could have altered the structure of the assessee's business and even the very existence of the company would have been threatened and, therefore, the expenditure thus incurred should have been held to be an expenditure for carrying on the business and thus allowable under section 37(1) of the Act which contention, however, was rejected by the Tribunal relying upon the decision of this court in Padmavati [1987] 166 ITR 176. In Padmavati's case (1987) 166 ITR 176, this court held that meeting the liability of income-tax was a personal one and the dominant purpose for paying annuity deposit was not to earn income but to meet the statutory liability of making the deposit. It was further held that the expenditure thus made was not

wholly and exclusively or the purpose of earning income and, consequently, the interest, which was paid to discharge the aforesaid tax liability was not allowable under section 57(iii) of the Income-tax Act, 1961. In Madhav Prasad's case [1979] 118 ITR 200, this court also came to the conclusion that in order to enable an assessee to claim deduction in respect of the interest on borrowed capital under section 10(2)(iii) of the Indian Income-tax Act, 1922, three conditions are required to be satisfied; namely,

(1) that money must have been borrowed by the assessee;

(2) that it must have been borrowed for the purpose of business; and

(3) that the assessee must have paid interest on the said amount and claimed it as a deduction.

It was further held that the payment made by the assessee by drawing a cheque on the overdraft account was a borrowing which was made to meet her personal obligation and not the obligation of the business and as such expenditure incurred by the assessee by way of payment of interest thereon was not for carrying on the business and consequently the said expenditure could not be regarded as business expenditure. In the aforesaid case, the overdraft in question had been made by the assessee to discharge her personal obligation in pursuance of a promise made by her to donate a sum of Rs. 10 lakhs for starting an engineering college and the question of payment of income-tax liability did not arise in that case. The case, therefore, is not of any direct assistance to the present case. But the principle laid down therein, namely, if capital is borrowed to meet the personal obligation of the assessee and not for the obligation of the business, then the expenditure cannot be regarded as a business expenditure would apply. As has been already noticed in Padmavati's case [1987] 166 ITR 176, this court had affirmatively held that meeting the liability for income-tax was a personal liability and such expenditure can never be held to be wholly and exclusively for the purpose of earning income.

In the aforesaid premises and in view of the question that arose out of the order of the Tribunal and which was referred by the Tribunal to the High Court for being answered, we find no error in the answer given by the High Court. It may further be stated that even before the High Court the assessee had not taken any step to get the question referred in the light of the contentions which were advanced in this court by filing an application under section 256(2) of the Act. In this view of the matter, notwithstanding the fact that we find considerable force in the question of law urged by Mr. Bhattacharyya, learned counsel appearing for the appellant, but, on the materials on record and on the amplitude of the question which had been referred to the High Court, we find it difficult to entertain and decide the contention raised by learned counsel for the appellant. Further, we do not find any error in the answer given by the High Court to the question posed before it and, therefore, the appeal is devoid of merit and the same is accordingly dismissed. But, in the circumstances, there will be no order as to costs.