

BOMBAY HIGH COURT

Ormerods (India) Private Ltd

Vs

Commissioner of Income-Tax

(K Desai, C.J. S.T Desai, J.)

27.10.1958

JUDGMENT

S.T. Desai, J.

1. On this reference arise a very short question of the construction of the first part of section 12(2) and the case, as aptly observed by the Tribunal, is rather extraordinary. The assessee is a private limited company. Its accounting year ends on 30th November every year. The reference has been brought in respect of an order affecting the assessment of the company of the years 1949-50 and 1950-51. It may be pointed out that the order relates to assessment not only of the two years 1949-50 and 1950-51 but to five years commencing with the assessment year 1949-50. In respect of the other three years, the Department has not raised any question for determination by the court. The balance-sheet of the company of the year ending 30th November, 1948, showed that it held total investment in share to the tune of over Rs. 521/4 lakhs. The assessee purchased a block of shares in Gannon Dunkerly & Co. Ltd. for a sum of about Rs. 521/2 lakhs during the accounting year ending with 30th November, 1948. There is no dispute that for the payment of the price of these shares, the assessee borrowed about 36 lakhs from the Empire of India Life Assurance Co. Ltd. and as security pledged these shares of Gannon Dunkerly & Co. Ltd. which it had purchased. In addition to this loan of Rs. 36 lakhs, the assessee also incurred other debts and the unsecured loans amounting to about Rs. 131/2 lakhs. That these moneys taken on loan from the insurance company and other persons were utilised for paying consideration of the shares is not in dispute. The paid up capital of the company is Rs. 5 lakhs and its total assets showed in the balance-sheet are about Rs. 64 lakhs including the shares already mentioned. In the previous years relevant to the two assessment years, the assessee paid sums of Rs. 1,69,085 and Rs. 2,04,333 respectively as interest on the capital borrowed for the purchases of the shares. During the relevant years, there was no income at all from those shares and the assessee claimed to set off these payments of interest against its other income in respect of the relevant assessment years. The Income-tax Officer dismissed the claim observing as under :

"I therefore, come to the conclusion that the investments made by Ormerods (India) Ltd. is not for a proper business consideration nor for sound investment consideration. This is purely a transaction in which the company, acquiesced in the personal financial transaction of the Gupta and Morarka Families. I, therefore, disallow the interest paid on these overdrafts in the computation of profits."

2. The Appellate Assistant Commissioner also took the same view and the assessee carried the matter in appeal to the Tribunal. The Tribunal held that the investment by the assessee in the shares of Gannon Dunkerley & Co. Ltd. was not a business venture. On a fair reading of the statement of the case and the order of the Tribunal, it is clear to us that the Tribunal has treated this purchase by the assessee company as "investment" by the assessee in the shares of Gannon Dunkerley & Co. Ltd. It rejected the claim of the assessee for set off on the ground which we may set out in the words used by the Tribunal itself :

3. In other words the total interest paid by the assessee arises on account of money which has been specifically utilised in the purchases of shares of Gannon Dunkerley & Co. Ltd. and Tupshied (Pakistan) Ltd. The investment in the second mentioned company of only Rs. 60,000. We are satisfied that these shares do not seem to have been purchased with a view to trade in them. One Gupta and Morarka had purchased these shares in partnership. As these persons controlled the appellant company the shares were transferred to the appellant company and then taken back after some time. The assessee company appears, to have served one purpose and that is the convenience of the interested parties."

4. Then the Tribunal goes on to hold that the interest was not allowable deduction under section 10(2)(iii) of the Income-tax Act. Then it adds :

"If, however, any income occurs on the shares or is deemed to accrue on these shares under interest has to be allowed under section 12. As we have stated hereinbefore, the loans have been specifically utilised for making investment in the abovementioned shares."

5. It will be noticed that the Tribunal has used here also the expression "investment" in respect of the purchases of these shares by the assessee company. The Tribunal proceeds to state in its order :

6. We are unable to understand the stand taken by the Department that as dividend income is deemed to have accrued to the assessee, interest cannot be allowed. We also do not agree with the Department that the assessee was a dummy holder of the shares. How can it be a dummy holder when the actual loans are taken by the assessee company by pledging the shares. It may be that the assessee company is holding these shares for the convenience of a third party. But at the material time it is the owner who has the beneficial interest in the shares."

7. It may be pointed out that at all material times the ownership as well as the beneficial interest in these shares was vested in the assessee company which had incurred liabilities specifically for the purpose of buying these shares. Then the Tribunal has expressed the view :

"The dividend income on these investments is not the business income of the assessee company..... If any dividend income is included in the appellant's assessment the interest should be allowed against such dividend income."

"Whether on the facts and in the circumstances so the case interest paid on money borrowed for the purchases of shares in Gannon Dunkerley & Co. Ltd. which did not yield any dividend income, could be set off against other income under section 24(1) of the Income-

tax Act ?"

8. At the very outset of his argument, Mr. Palkhivala, learned counsel for the assessee, stated that he did not intend to rely on any argument founded on the application of section 10(2)(iii). He has relied primarily on the right to set-off enunciated and laid down in section 24(1) and the provisions of section 12(2). The relevant part of these section is an under :

"24. (1) Where any assessed sustains a loss of profits or gains in any year under any of the heads mentioned in section 6, he shall be entitled to have the amount of the loss set off against his income, profits or gains under any other head in that year."

"12. (2) such income, profits and gains shall be computed after making allowance for any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of making or earning such income, profits or gins and further in the case of any income by was of dividend, for any reasonable sum paid by way of commission or remuneration to a banker or any other person realising such dividend on behalf of the assessee, provided that no allowance shall be made on account of....."

9. The brief argument of rounded on section 24(1) is that it presupposes and postulates a loss under every had of profits or gains set out in section 24. As a broad general proposition, we agree that such is the effect of section 24, though it would be necessary in dealing with each particular case under a particular head to examine the language of other relevant particular case under a particular head to examine the luggage of other relevant section referring to heads of income. The argument has also been that on a proper reading of section 12(2) - the section which deals with "other sources" - the real question of the consideration of the Tribunal was whether the borrowing was incurred by the assessee company solely for the purpose of making or earning income, profits or gins. The argument has proceeded that the departmental authorities were in error when they stressed one aspect of the case, viz., that no dividend income at all had been earned by the assessee company during the relevant years. It has been said that there is weighty authority for the proportion that to bring a case within the submit of the words authority for the proposition that to bring a case within the ambit of the words "incurred solely for the purpose of making or earning such income, profits or gains" it is not necessary that there should have resulted any income to the assessee company. It is not necessary that income should in fact have been earned in the accounting year as a result of that borrowing or any expenditure of a like nature to bring the case within the meaning of that expression. Mr. Palkhivala has also drawn our attention to certain observations made by the Supreme Court in Eastern Investment Co. Ltd. v. Commissioner of Income-tax. In that case, their Lordships held that the transaction before them was of such a nature as would fall within the purview of section 12(2) and the interest paid would be an allowable deduction under the sub-section. In the course of the judgment, it has been observed :

"It is not necessary to show that the expenditure was a profitable one or that in fact any profit was earned."

10. Sub-section (2) does not say that the deduction is permissible when any income has been earned or profits or gins made. All that it speaks of is that the expenditure must have been laid out solely for the purpose of earning income. There is nothing in the language of the section to suggest that the purpose needs to be fulfilled nor is it necessary that the purpose should fructify

into any benefit to the assessee by way of return in the shape of income. There is considerable force in the argument presented on behalf of the assessee.

11. On the other hand, it has been urged before us by Mr. G. B. Joshi, learned counsel for the Revenue, that the vital question for the court under section 12(2) is : For what purpose were these moneys borrowed ? That, it was said was a question of fact. So far we are in agreement with Mr. Joshi. Then, Mr. Joshi says that there are findings of fact of the Tribunal which are conclusive and decisive of the whole matter. Counsel has relied on the following words to be found in the order of the Tribunal :

"We are satisfied that these shares do not seem to have been purchased with a view to trade in them."

12. We have already mentioned that Mr. Palkhivala has not argued his case under section 10 which deals with income from business. The counsel has relied and relied very strongly on what the Tribunal has next stated :

"One Gupta and Morarka had purchased these shares in partnership. As these persons controlled the appellant company the shares were transferred to the appellant company and then taken back after some time. The assessee company appears to have served one purpose and that is the convenience of the interested parties."

13. It has been strenuously urged that the Tribunal has recorded an express and explicit finding that the purpose of these borrowings was not earning of any income or profits or gains by the assessee company but something fraudulent, viz., the convenience of the interest parties whose names are mentioned as Gupta and Morarka. The short argument of Mr. Joshi is that there is a clearly recorded finding of fact as to what the purpose of this borrowing was and it is said that the only answer that can be given on the question before us must, therefore, be against the assessee. We are unable to acquiesce in this argument. It is indubitably true that the Tribunal has stated that the purchase of these shares by the company has served the purpose of giving facility or convenience to two interested parties. It is equally true that the Tribunal has used the word "purpose" in recording this finding. Evidently there is here the use of an expression which has more than one meaning. "Purpose" may in some context suggest object; and purpose may sometimes suggest motive for a transaction. But under section 12, we have to read the word "purpose" in its legal sense to be gathered from the context in which it appears. We have to find out the meaning as far as possible from the language of the section itself and without attributing to the Legislature a precise appreciation of the technical appropriateness of its own. But whatever way we read the word "purpose" it cannot certainly mean a motive for a transaction. Much less can it mean the ulterior motive or the ultimate object of purchasing the shares by the company. The only possible way to read what Mr. Joshi has described as the express and explicit finding of the Tribunal is, in our opinion no more than a finding by the Tribunal as to the ulterior motive or ultimate object in purchasing the shares. But the purpose of the purchase is a different matter. All that the Tribunal has recorded is that the shares were not purchased with a view to trading in them. Incidentally, we may mention that the Income-tax Officer had observed that the investments were not for a proper business consideration nor for any "sound investment consideration". But we are concerned with the finding of the Tribunal and not what the Income-tax Officer may have said. There is, therefore, in our view no finding by the Tribunal that these

shares were not purchased solely for the purpose of making or earning income, profits or gains. Now the Tribunal has found that these purchases were investments of the assessee company. On the facts of the case and the finding recorded by the Tribunal the only possible conclusion that we can reach is that these investments were made for the purpose of earning income or dividends or for making profits or gains. In our opinion, the Tribunal has mixed up the concept of the purpose of the purchase of these shares by the company and what in its judgment was the motive for the purchase of the shares. It follows from the order of the Tribunal, part of which we have already set out that the Tribunal took the view that the assessee was entitled in respect of the three subsequent years to set off the payment of interest on the loans against the dividend income. That the purchase of the shares was to earn income would seem to be the very basis of that part of the order made by the Tribunal. In our judgment, where the Tribunal has gone wrong is that it has, while appreciating the nature of the purchase of the shares by the assessee company, given overriding effect to what it concluded was the motive for the purchase of the shares. The motive for the purchase of the shares and the purpose for purchase of the same should not have been allowed to be mixed up in that manner.

14. In the course of his argument Mr. Joshi has stressed that the capital of the company was only Rs. 5 lakhs and a company with a capital of Rs. 5 lakhs cannot have investments of Rs. 521/4 lakhs. We are unable to accept that argument. The question is not of the capacity of the company. The question is what was the purpose of these investments which in fact have been made by the company. It is also said that the purpose of the company was not investment but something fraudulent. It is said that it was implicit in the order of the Tribunal that these were fraudulent transactions. There is nothing about fraud in the reference before us and we do not propose to examine that argument. We do not know whether any loss was caused to the company or to any one as a result of the convenience or facility which, according to the Tribunal, was given by the assessee to Gupta and Morarka. It is difficult to see how any argument founded on fraud can stand on this reference. There has been some suggestion that the purpose of the borrowing may be said to be to increase the capital of the company. There is little scope for any such argument on this case.

15. Mr. Joshi has relied on a decision of the Patna High Court in Maharajadhiraj Sir Kameshwar Singh v. Commissioner of Income-tax. In that case one of the points to be determined by the court was whether interest paid by an assessee in his overdraft account on moneys borrowed for payment of call money on shares in companies which were new and which had not declared dividends could be treated as expenditure incurred solely for the purpose of making or earning income. The decision of the court was that no deduction was permissible to the assessee in respect of payment of such interest. At page 389 of the report, it is mentioned that the Appellate Assistant Commissioner had found that the assessee had paid the call moneys on shares in companies which were new and which had not declared dividends and as such there was no income to the assessee whatever from those sources and, therefore, if there was no such income that had inseparable connection with the interest payment, no deduction for interest was permissible. The question, it seems, was not argued before the Tribunal in that case. All that the Tribunal did was that in its statement of the case it mentioned the facts as they emerged from the finding of the Income-tax Officer. All that the judgment of the High Court states is that the decision of the Tribunal on this question is correct and the Income-tax Officer had rightly disallowed the deduction. We have often said in this court that in dealing with an enactment of all India importance and particularly the Indian Income-tax Act, we would, as far as possible, prefer

to take the same view that may have been taken by any other High Court on the interpretation of any section in that enactment. But with respect we are unable to agree with the conclusion stated in the judgment of the Patna High Court.

16. Before parting with the case we would like to observe that we agree with the observation of the Tribunal that this is rather an extraordinary case. The attitude of the Department also appears to us to be rather extraordinary in respect of the three subsequent years. The appeal before the Tribunal, as we have already mentioned, related to the five assessment years. In respect of the last three assessment years, no reference has been sought by the Department. In the two assessment years to which this reference relates, there was admittedly no dividend income realised by the assessee company from the purchase of those shares. The only inference that is possible is that according to the Department the effect of section 24 read with section 12(2) is that though income from dividend in a case of the nature us would be taxed under the head of other sources, if interest was paid on any loan incurred for the purpose of making the investment such interest would not be taken into computation. Of course, we are not concerned with any equitable consideration or any consideration of fairness while interpreting the provisions of the Act and if the language of section 12(2) compelled us to take the view urged on behalf of the Department, we would certainly take that view though not without some reluctance.

17. Our answer to the question will be in the affirmative.

18. Commissioner to pay the costs.

19. Question answered in the affirmative.