Commissioner of Income Tax Vs Kedraj Agricultural Industries

Court: Gujarat High Court

Date of Decision: Sept. 12, 2000

Acts Referred: Income Tax Act, 1961 â€" Section 28, 280O, 29, 30, 31

Citation: (2001) 171 CTR 23 : (2002) 253 ITR 346 : (2002) 121 TAXMAN 590

Hon'ble Judges: D.M. Dharmadhikari, C.J; Anil R. Dave, J

Bench: Division Bench

Advocate: B.B. Naik and Manish R. Bhatt, for the Appellant;

Final Decision: Dismissed

Judgement

A.R. Dave,J.

1. At the instance of the Revenue, the following two questions of law have been referred to this court for its opinion by the income tax

Appellate Tribunal, Ahmedabad Bench ""B"", under the provisions of Section 256(1) of the Income Tax Act, 1961 (hereinafter referred to as ""the

Act"").

1. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in coming to the conclusion that for the purposes of

calculating relief u/s 80HH of the Income Tax Act, 1961, the gross profit has to be determined after including therein interest/salary paid by the

assessee to its partners which are disallowable u/s 40(b) of the Income Tax Act, 1961 ?

2. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in coming to the conclusion that the order of rectification

passed u/s 154 of the Act by the Income Tax Officer was liable to be cancelled ?

2. We have heard learned counsel, Mr. Naik, appearing for the Revenue. None has appeared for the assessee.

3. The facts giving rise to the question pertaining to the present case are as under :

The assessee is a partnership firm. For the assessment years 1977-78 to 1979-80, the assessee was entitled to a deduction from its profits and

gains of an amount equal to 20 per cent, thereof under the provisions of Section 80HH of the Act. As the questions referred to hereinabove are

common for all the assessment years, so as to illustrate the facts, we shall look into the relevant figures of income, etc., pertaining to the assessment

year 1979-80 as the Tribunal has also referred to the factual details of the said year.

4. For the assessment year 1979-80, the Assessing Officer restricted the claim u/s 80HH of the Act to Rs. 85,103, being the divisible income as

determined prior to the adjustment of interest, which was paid to the partners of the assessee-firm, which was disallowed under the provisions of

Section 40(b) of the Act. It is interesting to note that the assessee-firm had paid an amount of Rs. 93,558 by way of interest to its partners. The

said amount was initially deducted from the profit of the assessee-firm as an expenditure but the said expenditure had been disallowed by the

Assessing Officer under the provisions of Section 40(b) of the Act.

5. As the Assessing Officer did not add the sum of Rs. 93,558, the amount paid to the partners which was disallowed, to the amount of divisible

profits for the purpose of giving benefit u/s 80HH of the Act, the assessee had filed an appeal before the Commissioner of Income Tax (Appeals).

The Commissioner of Income Tax (Appeals) dismissed the appeal and, therefore, the assessee was constrained to approach the Tribunal. The

Tribunal had allowed the appeal and had observed that the assessee could not have been deprived of the benefit under the provisions of Section

80HH, so far as the amount of Rs. 93,558 was concerned and had directed the Assessing Officer to give the said benefit to the assessee.

6. In the circumstances stated hereinabove, at the instance of the Revenue, the question which has been referred to this court is whether the amount

of interest paid by assessee-firm to its partners can be included in the profits of the assessee for the purpose of determining the benefit to be given

to the assessee-firm under the provisions of Section 80HH.

7. Section 80HH, at the relevant time read as under :

Where the gross total income of an assessee includes any profits and gains derived from an industrial undertaking, or the business of a hotel, to

which this section applies, there shall, in accordance with and subject to the provisions of this section, be allowed, in computing the total income of

the assessee, a deduction from such profits and gains of an amount equal to twenty per cent, thereof.

8. Upon a perusal of the said section, it is clear that while computing the gross total income of the assessee, a deduction of an amount equal to 20

per cent, from the profits and gains of the assessee, as determined in accordance with and subject to the provisions of this section, is to be

allowed.

9. Thus, for the purpose of determining the amount of deduction from the gross total income of the assessee, first of all the Assessing Officer has to

determine the gross total income of the assessee. The said gross total income has to be determined in accordance with and subject to the

provisions of the said section.

10. The term ""gross total income"" has been defined u/s 80B(5). At the relevant time, the term ""gross total income"" meant, the total income

computed in accordance with the provisions of the Act, before making any deduction under Chapter VI-A or u/s 280-O.

11. Thus, for the purpose of determining the gross total income of the assessee, the Assessing Officer has to compute the gross total income of the

assessee as per the provisions of the Act. The relevant sections for the purpose of determining the gross total income under the head ""Profits and

gains of business or profession"" were Sections 28 to 44D. Thus, the provisions of Section 40(b) had to be considered by the Assessing Officer for

the purpose of determining the gross total income of the assessee.

12. As per the provisions of Section 40(b) of the Act, in the case of any firm, certain amounts are not to be deducted in computing the income

chargeable under the head ""Profits and gains of business or profession"". Subject to the provisions of the said section, interest paid to the partners is

one of such amounts which is not to be deducted. Thus, if any amount is paid by the assessee-firm by way of interest to its partners, subject to the

provisions of the said section, the amount of interest so paid is not to be deducted as an expenditure for the purpose of computing the income

chargeable under the head of ""Profits and gains of business or profession"".

13. Looking to the provisions of the Act referred to hereinabove, it is crystal clear that the amount of interest, which was paid by the assessee-firm

to its partners, which was not allowable as an expenditure, could not have been deducted as expenditure from the gross total income of the

assessee or in other words, the said amount of interest paid to the partners of the assessee was not to be deducted as an expenditure and that

amount was to be treated as a part of the total income of the assessee.

14. As a result of the aforesaid fact, the amount which was paid to the partners of the assessee-firm by way of interest would be treated as part of

the ""profits and gains of business or profession"" and, therefore, the assessee-firm would be entitled to a deduction of 20 per cent, as per the

provision of Section 80HH of the Act even on the said amount of interest as it was not an allowable expenditure as per the provisions of Section

40(b) of the Act.

15. In our opinion, the Assessing Officer had committed an error by not allowing deduction to the tune of 20 per cent, on the amount of interest as

per the provisions of Section 80HH of the Act read with Sections 80B(5) and 40(b) of the Act. The Tribunal had rightly given benefit under the

provisions of section 80HH to the assessee by allowing deduction to the tune of 20 per cent, of the amount of interest which was paid by the

assessee to the partners, as the said amount was forming part of the ""profits and gains of business or profession"".

16. Thus, we are of the view that for the purpose of calculating relief u/s 80HH of the Act, the gross profit is to be determined after including

therein the amount of interest/salary which might have been paid by the assessee-firm to its partners and disallowed under the provisions of Section

40(b) of the Act. We, therefore, answer the first question in the affirmative and in favour of the assessee and against the Revenue.

17. The second question with regard to the validity of the order of the Tribunal cancelling the order of rectification passed u/s 154 of the Act by the

Income Tax Officer, referred to us at the instance of the Revenue, is also answered in the affirmative and in favour of the assessee and against the

Revenue.

18. Thus, both the questions are answered in the affirmative, and in favour of the assessee and against the Revenue. The reference thus stands

disposed of with no order as to costs.