Commissioner Of Income Tax, West Bengal-II, Calcutta Vs The East India Hotels Ltd., Calcutta

Court: Calcutta High Court

Date of Decision: Sept. 14, 1992

Acts Referred: Income Tax Act, 1961 â€" Section 256

Citation: (1993) 2 CALLT 348 : (1994) 207 ITR 881 : (1995) 82 TAXMAN 69

Hon'ble Judges: Shyamal Kumar Sen, J; Ajit Kumar Sengupta, J

Bench: Division Bench

Judgement

A.K. Sengupta, J.
In this reference made at the instance of the Revenue, the following questions have been referred by the Tribunal for the

opinion of this Court u/s 256 of the Income Tax Act, 1961:

Whether, on the facts and in the circumstances of the case, the Tribunal was correct in law in holding that the royalty of Rs. 3,43,600 was

allowable in the assessment year 1972-73 ?

Whether, on the facts and in the circumstances of the case while restoring the issue to the income tax Officer relating to the determination of the

chargeable head of the interest accrued on fixed deposits, the Tribunal was justified in law in observing that the earning of interest on the fixed

deposits could not be isolated from paying of interest by the assessed or the deposits received from the public?

If the answer to question No. 2 above is in the affirmative, then whether the Tribunal was correct in law to hold that the interest accrued on fixed

deposit should be assessed under the head ""Business Income""?

2. This reference relates to the income tax assessment of the assessee-company for the financial year ending 31st March, 1972, being the previous

year relevant to the Assessment Year 1972-73. The facts as found by the Tribunal are as under :

3. In terms of an Agreement executed between the assessee-company and Oberoi Hotels (India) Pvt. Ltd. on 15th June, 1972, the hotels owned

by the assessee-company became entitled to use the name ""Oberoi"" against payment of compensation calculated @ Rs. 600/- per Guest Room

per year. This Agreement was effective from-1st April, 1970. The previous year of the assessee-company for the matter under reference ended on

31st March, 1972 ; but the audit of accounts for the relevant previous year was completed and finalized sometimes in August, 1972. While

finalizing the accounts for the year ending 31st March, 1972, the assessee-company made provision for payment of royalty in the sum of Rs.

6,91,200/- in terms of the said Agreement executed on 18th May, 1972. This provision was made for the period 1st April, 1970 to 31st March,

1972. This income tax Officer allowed deduction in the sum of Rs. 3,45,600/- for the period 1st April, 1971 to 31st March, 1972, corresponding

to the Assessment year 1972-73. but he did not allow any deduction for the balance sum of Rs. 3,45,600/- relating to the period 1st April, 1970

to 31st March, 1971 on the ground that although the assessee maintained accounts on mercantile basis, it did not give my suitable explanation for

not charging this sum of Rs. 3,45,600/- in the immediately preceding year, that is to say, previous year relevant to the Assessment Year 1970-71.

The disallowance made by the Income Tax Officer was later confirmed on appeal by the Commissioner of Income Tax (Appeals). The assessee

filed second appeal to the Income Tax Appellate Tribunal. It was submitted before the Tribunal on behalf of the assessee that it was using the word

Oberoi"" in terms of the resolution passed on 11th August, 1970. But no payment of royalty could be made without approval of the Industrial

Finance Corporation of India from whom assessee company had borrowed certain funds. The formal Agreement for payment of royalty to Oberoi

Hotels (India) Pvt. Ltd. could be executed only on 15th June, 1972 after obtaining the approval of the Industrial Finance Corporation of India

through its letter dated 18th May, 1982. The Tribunal noted that the accounts for the previous year relevant to the Assessment year 1972-73 now

in reference before us were finalized and signed only on 22nd August, 1972. Since the Agreement providing for payment of royalty with

retrospective effect from 1st April, 1970 had already been signed on 15th June, 1972, the entire royalty relating to the period 1st April, 1970 to

31st March, 1972 was rightly provided in the accounts for the year ending 31st March, 1972 following the publication of the Institute of Chartered

Accountants of India titled ""Contingencies & Events occurring after the Balance Sheet date"".

4. In this view of the matter, the Tribunal directed that the liability of Rs. 3,45,600/- relating to the period 1st April, 1970 to 31st March, 1971

was rightly allowable as a Business Expenditure in the assessment for the Assessment year 1972-73.

5. We have not been able to appreciate the reasoning given by the Tribunal for accepting the claim made by the assessee in respect of the

deduction for Rs. 3,45,600/-. It is an undisputed fact that this sum related to the royalty payment for the immediately preceding previous year

commencing on 1st April, 1970 and ending on 31st March, 1971. The assessment under reference is for the previous year commencing on 1st

April, 1971 and ending on 31st March, 1972. The liability for the preceding year which arose as a result of the Agreement admittedly executed on

15th June, 1972, can, by no stretch of imagination, be allowed as a business expenditure in the year under reference. The liability for payment of

expenditure by way of royalty arose as a result of the Agreement executed on 15th June, 1972. This can lawfully be claimed as a business

expenditure only in the previous year commencing on 1st April, 1972 and ending on 31st Much, 1973. The publication of the Institute of

Chartered Accountants of India titled ""Contingencies & Events occurring after the Balance Sheet date"" has nothing to do with the issue involved in

this reference. Since the Agreement between the assessee-company and Oberoi Hotels (India) Pvt. Ltd., under which the liability to pay royalty

arose could not have been admittedly executed without the approval of the Industrial Finance Corporation of India from whom the assessee-

company had borrowed certain funds and when admittedly the Industrial Finance Corporation of India granted approval to the proposed

Agreement only by its letter dated 18th May, 1982, the liability to pay the royally could have never accrued prior to the date of execution of the

Agreement.

6. In that view of the matter, we answer the first question referred by the Tribunal in this case in the negative and in favour of the Revenue.

7. Coming now to the other two questions referred by the Tribunal, we find that the only issue involved therein relates to the head of income under

which interest on fixed deposits should be assessed to income tax. In this respect, the Tribunal has recorded that the assessee-company was

accepting deposits from public in accordance with the provisions of Companies (Acceptance of Deposits) Rules, 1975. These deposits were

received and accepted by the assessee-company in the course of and for the purposes of business. Rule 3A of the Companies (Acceptance of

Deposits) Rules, 1975 requires every company to deposit or invest, as the case may be, a sum which shall not be less than 10% of the amount of

its deposits maturing during the year ending on the 31st day of March next following, in one or more methods specified therein. One of the modes

of investment specified in Rule 3A is deposit in a Current or other Deposit Account with any Scheduled Bank free from charge or lien. Sub-rule

(2) of Rule 3A further provides that the amount deposited or invested under sub-rule (1) shall not be utilised for any purpose other than for the

repayment of deposits maturing during the year referred to in that sub-rule. It was contended on behalf of the assessee-company before the

Tribunal that the interest payable by the assessee-company on the deposits accepted from the public under the Companies (Acceptance of

Deposits) Rules, 1975 have been allowed as business expenditure. The Tribunal noted that full facts were available from the order of the

Authorities below and, therefore, it was not in a position to finally decide the issue. The Tribunal observed that if the facts as stated by the

assessee-company were correct, the earning of income by way of interest on fixed deposits made by the assessee-company in pursuant to Rule

3A of the Companies (Acceptance of Deposits) Rules, 1975 could not be isolated from the payment of interest made by the assessee-company on

the aggregate deposits received and accepted by it from the public and admittedly used for the purpose of business.

8. In our view, the Tribunal was fully justified in taking the aforesaid view. Making of fixed deposits with the Schedule Bank to the extent of 10%

of the deposits accepted is a mandatory requirement under Rule 3A of the Companies (Acceptance of Deposits) Rules, 1975. The earning of

interest on such fixed deposit is directly incidental to the receipt and acceptance of the aggregate deposits from the public and payment of interest

thereon. The interest on fixed deposits in these circumstances must go to reduce the aggregate payment of interest made by the assessee-company

on the total deposits accepted under the said Rules. If the deposits are accepted and used for the purposes of business, the not expenditure by

way of interest on deposits after deducting from the gross interest the interest earned on the fixed deposits is a business expenditure. If the entire

payment on aggregate deposits is treated as business expenditure, the interest received on fixed deposits made under Rule 3A must be treated as

business income and assessed to tax under the head ""Profits & Gains of Business or Profession"".

In this view of the matter, we answer questions 2 and 3 in the affirmative and in favour of the assessee.

There will be no order as to costs.

S.K. Sen, J.

8. I agree.