

IN THE HIGH COURT OF PUNJAB AND HARYANA AT CHANDI GARH

INCOME TAX APPEAL No. 438 of 2006 (O&M)  
DATE OF DECISION: 03.10.2016

Smt. Sati sh Bal a Mal hotra

.... . Appel l ant

versus

Commi ssi oner of Income Tax, Jal andhar

..... Respondent

CORAM: - HON' BLE MR. JUSTICE S. J. VAZI FDAR, CHI EF JUSTI CE  
HON' BLE MR. JUSTICE DEEPAK SI BAL

Present: Mr. Pankaj Jain, Seni or Advocate wi th  
Mr. Di vya Suri , Advocate and  
Mr. Sachin Bhardwaj , Advocate for the appel l ant  
  
Mr. Vi vek Sethi , Advocate for the respondent  
..

S. J. VAZI FDAR, CHI EF JUSTI CE:

This is an appeal against the order of the Tribunal confirming the order of the Commissioner of Income Tax (Appeals) enhancing the appellant/assessee's income. The appeal pertains to the Assessment Year 1997-98. The Assessing Officer had disallowed interest of Rs. 9,45,675/- out of the total claim of interest of Rs. 18,91,335/-.

2. By an order dated 29.10.2007, the appeal was admitted on the following substantial questions of law: -

"i. Whether under the facts and circumstances of the case the interest on money borrowed for investment in shares in M/s M. Gulab Singh & Sons (P) Ltd. which had not yielded any dividends is admissible deduction?

- ii. Whether under the facts and circumstances of the case, Tribunal is justified that the shares have been purchased by appellant to acquire controlling interest and hence not allowable deduction?"

3. The assessee had claimed a deduction of Rs. 18,91,335/- on account of interest paid to the Ashok Kumar Malhotra HUF. Ashok Kumar Malhotra is the assessee's husband and the assessee is a member of the said HUF. The assessee claimed that she had borrowed funds from the HUF during the Assessment Year 1987-88 to purchase shares of M/s M. Gulab Singh & Sons Pvt. Ltd. (hereafter referred to as the "Company") and M/s M. B. D. Enterprises Pvt. Ltd. The Assessing Officer asked the assessee to furnish details of the investment out of the borrowed funds. As the assessee did not furnish the details, the Assessing Officer assumed that out of the borrowed funds investment to the extent of 50 per cent had been made for the purchase of the shares in these companies. He accordingly disallowed 50 per cent of the interest amounting to Rs. 9,45,660/- out of the total interest claimed.

4. The CIT(A) observed that the entire borrowed funds of Rs. 18,91,355/- had been used by the assessee for acquiring shares of the company M/s M. Gulab Singh & Sons Pvt. Ltd. and no part thereof was utilised for purchasing shares of M/s M. B. D. Enterprises Pvt. Ltd. Having held that the shares were purchased to acquire control of the company and not as an investment, the CIT (A) disallowed the entire amount of Rs. 18,91,355/-. The CIT (A) accordingly enhanced the

assessee's income by Rs. 9,45,660/- and ordered initiation of penalty proceedings under Section 271 (1)(C) for furnishing inaccurate particulars of income.

5. The Tribunal agreed with the CIT (A) that the entire funds were utilized for the purpose of purchasing the shares of the company and confirmed the order of the CIT (A) enhancing the income. The assessment order and the order of the CIT (A) did not furnish the details of the assessee's holding. The Tribunal's order, however, furnishes the details of the assessee's holdings.

6. The facts necessary for the determination of this appeal are these:

Ashok Kumar Malhotra HUF, Ashok Kumar Malhotra as an individual, M/s M. B. D. Enterprises Pvt. Ltd. and the assessee purchased 2459, 1495, 945 and 1933 equity shares in the company, respectively, aggregating to 6832 shares. The entire share capital of the company is held by them. The assessee, thus, purchased 28.29 per cent of the equity shares of the company. She is the wife of Ashok Kumar Malhotra and a member of his HUF as also a share-holder and a Director in M/s M. B. D. Enterprises Pvt. Ltd. She borrowed money from the Ashok Kumar Malhotra HUF for the purchase of these shares on interest. For the assessment year in question, she paid interest of Rs. 18,91,355/- in respect of which she claimed a deduction under Section 57 (iii).

7. Section 57 (iii), as it then stood, read as under: -

"57. The income chargeable under the head "Income from other sources" shall be computed after making the following deductions, namely: -

(iii) any other expenditure (not being in the nature of capital expenditure) laid out or expended wholly and exclusively for the purpose of making or earning such income;"

Re: Question (i):

8. The Tribunal firstly held that the assessee had not clarified that she had been in the business of dealing in shares and that unless the assessee proved that she had been dealing in shares as a business it was difficult to accept the contention that she purchased the shares for the purpose of making or earning income.

9. The assessee's income chargeable under the head "Income from other sources" is to be computed after making the deductions mentioned in Section 57 which under sub-section (iii) thereof includes any other expenditure not being in the nature of capital expenditure laid out or expended wholly and exclusively for the purpose of making and earning such income. The words "such income" refer to income from other sources. The deduction under Section 57 (iii) is not available only to persons who deal in shares as a business. Even other investors are entitled to the benefit of Section 57. The observation, that unless and until the assessee proves that she has been dealing in shares as a business it is difficult to accept the contention that the shares purchased by her are for the purpose of making and earning such income, is not well-founded. There is no presumption that a person not involved in the business of dealing in shares purchases them for a purpose other than making or earning income from such shares. There is certainly no presumption that such persons purchase shares for the purpose of gaining control of the company. In fact, a

Large number of persons purchase shares in various companies for the purpose of making or earning income therefrom than for purpose of gaining control of companies.

10. That a company in which the shares are purchased does not declare dividend even for a few years is not determinative of the purpose for which the shares are purchased. The receipt of dividend is not the only criteria. What is entitled to be deducted is the expenditure exclusively for the purpose of making or earning such income. If an assessee establishes that he has incurred expenditure for the purpose of making or earning such income, he is entitled to the deduction under Section 57(iii). It is not necessary that the expenditure laid out or expended actually results in making or earning such income. There are several companies which do not declare dividend in certain years. There are companies which do not declare income for several years and are ultimately wound up. That does not mean that the expenditure laid out or expended for the purpose of purchase of its shares was not wholly or exclusively for the purpose of making or earning income therefrom.

11. This point stands concluded by several judgments of the Supreme Court and various High Courts. It is sufficient to refer to a judgment of the Supreme Court under Section 12(2) of the Income Tax Act, 1922, which is similar to Section 57 (iii) of the 1961 Act and a judgment of the Supreme Court under the 1961 Act.

In *Eastern Investments Limited vs. Commissioner of Income Tax*, [1951] 20 ITR 1(SC), the Supreme Court held that

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

In Commissioner of Income-Tax, West Bengal -III vs. Rajendra Prasad Moody, [1978] 115 ITR 519, the Supreme Court held: -

"3. What s. 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 s. 57(iii) and that purpose must be making or earning of income. s. 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 s. 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 s. 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. CIT [1951] 20 ITR 1, 4 (SC), where interpreting the corresponding provision in s. 12(2) of the I.T. Act, 1922 which was ipsissima verba in the same terms as s. 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 s. 57(iii)."

12. Thus, the fact that no dividend is declared does not by itself indicate that the expenditure was not laid out or expended for the purpose of making or earning income.

The first question of law is, therefore, answered in favour of the appellant/assessee.

Re: Question(ii):

13. The observation in Moody's case that Section 12(2) of the 1922 Act is ipsissima verba takes us to the next point. It was observed that the corresponding provision of Section 12(2) of the 1922 Act is Section 57(iii) of the 1961 Act and that Section 12 (2) was ipsissima verba (in the same terms) as Section 57(iii). Section 12(2) of the 1922 Act, in so far as it is relevant, read as under: -

"12. Other sources. -

(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 gains."

Section 12(2) used the word "solely" whereas section 57(iii) uses the words "wholly and exclusively". It seems to us that there is no qualitative difference on account of the use of the words "wholly and exclusively" in place of the word "solely". The Legislature appears merely to have emphasized the point rather than expanded the scope of the section. This is clear for more than one reason.

14. Firstly, the Supreme Court itself held in Moody's case that section 12(2) is ipsissima verba as section 57(iii) of the 1961 Act. The Latin expression ipsissima verba means "the very words". Although the very word "solely" is not used in section 57(iii) which uses the words "wholly and exclusively", the Supreme Court considered the scope of the two sections to be the same.

15. Secondly, the Notes on Clauses with respect to section 57(iii) published on 24.04.1961 in the Gazette of India (Extraordinary), Part II-Section 2, page 243, states: -

"Item (iii).- The expression "solely for the purpose...." occurring in the existing section has been substituted by the words "wholly, necessarily and exclusively for the purpose...." to secure uniformity with the language adopted elsewhere in the Bill."

The Notes on Clauses do not indicate any qualitative difference on account of the words "wholly and exclusively" in section 57(iii) of the 1961 Act substituting the word "solely" in section 12(2) of the 1922 Act. The words were used only to secure uniformity with the language adopted elsewhere in the Bill.

16. Thirdly, each of these words - "solely", "wholly" and "exclusively" are synonymous to each other. Almost every dictionary and law lexicon suggests this. In Corpus Juris Secundum, Volume 33 Page 113, it is stated that the term "exclusively" has been held equivalent to or synonymous with "solely" and "wholly". Corpus Juris Secundum, Volume 81 at page 387 states that the word "solely" is defined as meaning "exclusively" and "wholly". It states that the word "solely" has been held equivalent to or synonymous with "exclusively" and "wholly". Corpus Juris Secundum, Volume 94 at page 15 states that the word "wholly" has been held to be equivalent to or synonymous with "exclusively" and "solely".

17. This brings us to the interpretation of section 57(iii) in so far as it is relevant to this appeal. The main question that calls for consideration is whether the assessee acquired these shares to gain control or whether she acquired

them as an investment. The Tribunal upheld the finding of the Assessing Officer and of the CIT (A) that the assessee's real intention was to hold and acquire control over the company-M/s M. Gulab Singh & Sons Pvt. Ltd.

18. Decided cases have cautioned against mistaking the purpose of expenditure laid out or expended for making or earning such income with the motive for doing so. The judgments have emphasized the difference between the purpose of the expenditure being laid out or expended and the motive for the expenditure being laid out and expended. If the expenditure is laid or expended for the purpose of making or earning such income, the assessee is entitled to the benefit of section 57(iii) irrespective of the motive for doing so.

19. In Ormerods (India) Private Ltd. vs. Commissioner of Income-Tax, Bombay City, [1959] 36 ITR 329 (Bom), the assessee purchased a block of shares in Gannon Dunkerley & Co. Ltd. for a sum of Rs. 52.25 lacs. Rs. 36 lacs was paid from a loan granted by Life Assurance Company Limited against a pledge of those shares. The assessee also incurred other debts and obtained other loans aggregating to Rs. 13.50 lacs for the purchase of the shares. The loans were utilized for paying the consideration of the sharers. The assessee paid interest in the previous year aggregating to about Rs. 3,73,000/-. There was no income from those shares. The assessee claimed to set off the payment of interest against its other income. One Gupta and one Morarka controlled the assessee company and had purchased these shares in partnership. They transferred the shares to the assessee and took the same back after some time.

The ITO rejected the claim observing that the investment was not for a proper business consideration and was purely a transaction in which the company acquiesced in the personal financial transactions of the Gupta and Morarka families. The Appellate Assistant Commissioner confirmed this view. The Tribunal held that the assessee had served one purpose and that was the convenience of the said Gupta and Morarka. Paragraphs 5 and 11 of the judgment read as under: -

"5. The question which we have to determine on this reference is:

"Whether on the facts and in the circumstances of the case interest paid on moneys borrowed for the purchase 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?"

11. 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 interested 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 some times 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."

20. In Seth R. Dalmia vs. The Commissioner of Income Tax, Delhi, New Delhi, (1977) 4 Supreme Court Cases 329, the Supreme Court referred to the judgment of the Bombay High Court in Ormerods (India) Private Ltd. vs. Commissioner of Income-Tax, Bombay City, [1959] 36 ITR 329 (Bom) and C.I.T. vs. Vijaykuverba Saheb of Morvi, [1975] 100 ITR 67 (Bom). In that case also, the Supreme Court dealt with Section 12(2) of the 1922 Act. In paragraph 8, the Supreme Court observed: -

"Apart from these decisions of this Court, a number of decisions of the High Courts have also taken the same view. In Ormerods (India) Private Ltd. vs. Commissioner of Income-tax, Bombay City, 36 ITR 329 (Bom HC), the Bombay High Court allowed certain sums of money paid as interest on borrowed capital for the purchase of shares and held that the word "purpose" in the expression "expenditure incurred solely for the purpose of making or earning such income, profits or gains" did not mean motive for the transaction, much less can it mean ulterior motive or ulterior object. The Court held that as the investments were made for the purpose of earning income, the interest paid thereon would be deductible under Section 12(2) of the Act.

..... " . . . . . "

21. Mr. Jain also relied upon the judgment in Commissioner of Income Tax. Vs. H.H. Maharani Shri Vijaykuverba Saheb of Morvi & Ors, [1975] 100 ITR 67 (Bom), where the above proposition was reiterated. In that case, section 12(2) of the 1922 Act fell for consideration. He contended that section 12(2) was held applicable even if the expenditure was made to preserve the source of income. We are not concerned here with such a case.

22. The judgments, though under Section 12(2) of the 1922 Act, apply to cases under section 57(iii) of the 1961 Act

for as we held earlier, the two sections are to the same effect.

23. Mr. Sethi, the learned counsel appearing on behalf of the respondent submitted that the shares had not been purchased by the assessee for the purpose of making or earning income, but only for the purpose of controlling the company M/s M. Gulab Singh & Sons Pvt. Ltd. In support of his contention, he relied upon the fact that it is only members of the Malhotra group who had invested in the shares of the company.

24. Both the learned counsels proceeded on the basis that any expenditure laid out or expended to acquire shares for the purpose of controlling a company would not fall within the ambit of Section 57(iii). We, therefore, proceed on that basis without expressing an opinion on the correctness of the submission. The only question that falls for our consideration then is whether the assessee purchased the shares for the purpose wholly and exclusively of making or earning income or whether she did so for the purpose of acquiring control of the company.

25. Whether the acquisition of shares is for the purpose of making or earning income or whether it is to acquire or gain control over the company would depend upon the facts of each case. Further, considering the facts of this case, it is necessary to note certain aspects regarding the concept of control in relation to a company limited with shares.

26. Firstly, control itself is of different types and to a varying extent. We presume that what is meant by control of a company is the ability to control its management and affairs by virtue of the exercise of rights as a shareholder. A person, who holds 51 per cent of the equity shares, would be in a position to ensure that an ordinary resolution is passed or defeated. A person, who holds 75 per cent of the equity shares, can ensure that a special resolution is passed or defeated. A person, who controls over 90 per cent of the equity shares of a company, ensures that the other shareholders, even together, cannot maintain an action for oppression and mis-management under sections 397 and 398 of the Companies Act except with the permission of the Central Government. In a given case and depending upon the spread of the equity capital, a person may well be in a position to control the company with much less than 51 per cent of the equity shares. Once it is conceded that section 57(iii) is inapplicable where the purpose of acquisition of shares is to control a company and not to make or earn income, the proposition would apply irrespective of the nature or the extent of the control. We reiterate that we proceed on the basis of the said concession.

27. Secondly, the control need not necessarily be on account of the shares being held by a single shareholder. If more than one person holds the controlling interest in concert with others, i.e., with the common purpose of acquiring or maintaining control, each of them would be said to have acquired the shares for the purpose of acquiring or maintaining control. Whether the intention or the purpose was

to acquire control of a company or not would depend upon the facts of each case. For instance, if parties act in concert, each of them may acquire a relatively small percentage of the share. However, their aggregate holding may confer upon them a controlling interest. The purchase of shares by each of them would then be for the purpose of acquiring control over the company. Take for instance, a case where the members of a family hold 48 per cent of the equity share capital of a company. They could acquire a controlling interest by the acquisition of more than 2 per cent of the shares through another member of the family. This acquisition of more than 2 per cent could be a purchase for the purpose of gaining or maintaining control over the company and not for the purpose of investment. Merely because a new shareholder purchases only about 2 to 3 per cent of the shares of the company, it does not follow that the acquisition was not for the purpose of gaining control over the company.

28. Conversely, it is possible that an acquisition of shares is for the purpose of making and earning income. In such a case, if incidentally, a person, together with others in the group, acquires control over the company, it would not necessarily follow that the purchase is for the purpose of gaining control over the company. Merely because the acquisition of shares results in a person or a group of persons acquiring control of whatever nature and to whatever extent, it would not necessarily follow that the purpose of the acquisition was to gain control. That would again depend upon the facts of the case. If the expenditure is laid out or expended wholly and exclusively for the purpose of earning

dividends, the fact that the assessee incidentally also acquires control of a company for himself and/or for others would make no difference. He would be entitled to the benefit of section 57(iii) for the purpose for which the shares were acquired was making or earning income and not gaining control. In such a case, gaining control of a company would be purely incidental. It would not even be a motive. Even if it was the motive, it would make no difference so long as the shares were acquired wholly and exclusively for the purpose of making and earning income by way of dividend. This is so in view of the judgments in Ormerods (India) Private Ltd. vs. Commissioner of Income-Tax, Bombay City, [1959] 36 ITR 329 (Bom); Seth R. Dalmia vs. The Commissioner of Income Tax, (1977) 4 Supreme Court Cases 329 and C.I.T. vs. Vijaykuverba Saheb of Morvi, [1975] 100 ITR 67 (Bom), referred to earlier.

29. In the present case, as we noted earlier, the assessee had acquired about 28 per cent of the shares in the company M/s M. Gulab Singh & Sons Pvt. Ltd. That by itself would not establish that the shares were purchased for the purpose of acquiring control over the company. However, as we have also held, it is not an acquisition of over 50 per cent of the equity share capital alone that would allow gaining control over a company. The purpose of acquisition of shares must be ascertained after considering all the facts and circumstances of the case.

30. In the present case, the assessee acquired about 28 per cent of the shares in the company. It is true that the Malhotra group owns the entire shareholding in the company.

When a party buys shares in a company, it is reasonable to presume that it does so wholly and exclusively for the purpose of making or earning dividend income. If a party expects the company to do well presently or in future, it is but natural that it would seek to acquire as many shares as it can. This too would be wholly and exclusively for the purpose of making or earning income therefrom. Parties do not acquire control for control's sake. In the present case, the other members of the group held 72% of the equity shares. There is nothing to indicate that the assessee herself or in concert with others intended acquiring control for any reason. Our attention was not invited to anything that indicates any reason for the assessee acquiring the shares for the purpose of acquiring or even maintaining control. It is reasonable then to presume that the assessee acquired the shares wholly and exclusively for the purpose of making or earning income.

31. The Tribunal appears to have proceeded only on the basis that the entire shareholding of the company is held by the appellant along with other members of the group including her husband and her husband's HUF and the fact that the dividend had not been declared. There could always be prospects of the company doing well in future. Indeed, if that was not the expectation, the appellant would not have invested in the company at all. There is merely a finding that the real intention appears to be to hold and acquire the control of the company, as otherwise the assessee and the other family concerns, in which she is also interested, would not have invested large amount by way of investment particularly when the company had not declared any dividend. We observed earlier,

neither of these reasons by itself warrants the conclusion that the shares were acquired wholly and exclusively for the purpose of control and that they were not acquired wholly and exclusively for the purpose of making or earning income. In the facts and circumstances of this case, these two factors even taken together do not warrant the conclusion arrived at by the Tribunal.

32. Mr. Jain relied upon a judgment of a Division Bench of the Calcutta High Court in CIT vs. Model Manufacturing Co. (P) Ltd., [1980] 122 ITR 767. In that case, the appellant-assessee carried on business as a selling agent and also in speculation and other commodities. At the instance of one of its directors N.L. Kanoria, it purchased 10,100 shares in the New City of Bombay Manufacturing Co. Ltd. in the names of said N.L. Kanoria and Tulsi Das Kanoria who, in turn, sold the said shares to the assessee on the same date. The sellers were paid by borrowing from a concern M/s Tulsi Das Kanoria & Co. Further shares were also purchased by the assessee in the name of one Jhunjhunwala, a relative of theirs. The price of these shares was paid by taking another loan from the said M/s Tulsi Das Kanoria & Co. The question that arose was whether the interest on the amounts borrowed by the assessee for purchasing shares was allowable as business expenditure. The ITO found that the shares had been purchased with a view to acquiring controlling interest in the company for and on behalf of Kanorias. The ITO also found that in the subsequent assessment year the assessee had entered into further transactions in purchase and sale of these shares at cost price without profit or loss. The AAC confirmed the order. The Tribunal, however, did not agree with

the finding to the effect that interest should not be allowed against the assessee's income from other sources. The Division Bench also referred to the judgment in Ormerods (India) Private Ltd. (supra) and held as under: -

"21. It also appears to us that, even otherwise, the contention of the revenue cannot be sustained on merits in view of the decision of the Bombay High Court in the case of Ormerods (India) P. Ltd.'s case, [1959] 36 ITR 329, where the High Court made a clear distinction between motive and purpose on facts almost identical to those before us. This decision has been approved by the Supreme Court. We follow the said decision with respect and draw similar distinction between motive and purpose and hold that in the instant case, though the ultimate or ulterior motive of the assessee might have been to confer controlling interest either to itself or to the Kanorias, yet the immediate purpose for acquisition of the shares was to earn income from the dividends thereof. We add that even if the motive of the assessee might have been to obtain control of another company, the consequent purchase of shares may still be treated as investment and the concurrent purpose of the assessee could well have been that of earning further income by acquiring the control of the other company."

The judgment on facts applies with greater force to the present case where it is not even established that the motive and purpose of the assessee acquiring shares was to acquire or maintain the controlling interest. Having said that, it must be noted that the judgment really turned on the facts of the case. The Court analyzed the facts of the case in arriving at its conclusion. It is not for us to consider whether the analysis of the facts is correct or not and we refrain from doing so. Whether our analysis of the facts and perception thereof would be the same or not is irrelevant. The judgment, however, supports Mr. Jain's contention that while considering such a case, a distinction must be drawn between the purpose and the motive of an assessee in incurring the expenditure and expending the same.

33. Mr. Sethi, on the other hand, relied upon a judgment of the Division Bench of the Gujarat High Court in *Sarabhai Sons (P.) Ltd. vs. Commissioner of Income-Tax*, [1993] 201 ITR 464. In that case, the assessee derived income from its various activities including dealing in the products of its sister concern. It was a shareholder of Swastik Oil Mills Ltd, referred to therein as "SOML", and was also its managing agent. It held 11264 shares of SOML. Two other groups also held shares. The three groups decided that all the shares be held by the assessee to facilitate the implementation of an expansion project. The assessee acquired the shares at a price to be paid in instalments carrying interest at 10% per annum. The assessee encountered some difficulties in acquiring the balance shares of SOML from the other shareholders. A company Karamchand Premchand Pvt. Ltd. (KPPL) offered to purchase the shares of SOML from the assessee. The shares were sold to KPPL for which the consideration was to be paid in instalments carrying interest at 9% per annum. The assessee claimed the net deficiency in interest. The ITO was of the view that the expenditure was of capital nature and that the shares were acquired by the assessee only with a view to hand over the same to KPPL. The Tribunal held that the claim for deduction under Section 57(iii) for one of the assessment years was well founded as it derived dividend income but not for the other assessment year in which dividend had not been declared and because the assessee's obligation to make payment of interest to the shareholders of SOML was independent of the right to receive interest from KPPL and that it was, therefore, not possible to say that payment of interest was required to be

made by it to the shareholders of SOML in order to earn or derive income by way of interest from KPPL. The Division Bench held: -

"Now, if we turn to the facts of this case, what is required to be noted is that the shares of SOML were held by the assessee along with two other groups of shareholders, viz., Kasturbhai group and Patel group. The assessee held 11,264 shares, Kasturbhai group held 24,975 shares and the Patel group held 12,737 shares. The assessee was also the managing agent of SOML. It was agreed amongst the shareholders that the assessee should purchase all the shares in order to improve the business of SOML by holding 100% shares of SOML, which would have enabled it to implement the expansion projects. Thus, the shares which were purchased by the assessee were not for the purpose of earning income, though that can be regarded as the ultimate motive. The shares were purchased by the assessee with a clear purpose or object of getting 100% control over SOML. If the purpose was to earn income only, or even if that was the dominant purpose, it would not have sold the shares again to KPPL as, by that time, it had already acquired more than 90% shares, and that would have satisfied its object of earning more income by possessing more shares. The reason why the assessee sold the shares was that it was not able to get 100% control by purchasing all the remaining shares. Thus, from the nature of the transaction, it becomes apparent that the expenditure which was incurred by the assessee was not for the purpose of earning income, but for the purpose of getting full control over SOML. Thus, applying the test as laid down in Kasturbhai Lalbhai's case, [1968] 70 ITR 267 (Guj) and Smt. Virmati Ramkrishna's case, [1981] 131 ITR 659 (Guj) to the facts of this case, it becomes clear that the dominant purpose for which expenditure was incurred was not to earn income. At the highest, it was a mixed purpose. For that reason, it will have to be held that the expenditure incurred in that behalf fell outside the purview of section 57(iii) of the Act."

It is important to note that the decision turned on an appreciation of the nature of the transaction. The Division Bench found, as a matter of fact, that the investment had been made not for the purpose of earning income but for the purpose of taking full control over SOML. It was also found, as a

question of fact, that the shares were not purchased for the purpose of earning income, though that could be regarded as the ultimate motive. In other words, earning income, by acquiring the shares, was not the purpose but the motive. It was further found that the dominant purpose was not to earn income but to gain control and, at the highest, it was a mixed purpose. The judgment, therefore, does not carry the matter further as far as this appeal is concerned.

34. Mr. Sethi then relied upon a judgment of a Division Bench of the Bombay High Court in Commissioner of Income-Tax vs. Amritaben R. Shah, [1999] 238 ITR 777. It was a reference on the question whether the assessee was entitled to a deduction under Section 57(iii) of the interest on the loans raised for acquiring shares in Raval Tiles and Marbles Pvt. Ltd. with an intention to acquire control over the company. The assessee, her husband and her father-in-law purchased the entire share capital of the company. The Assessing Officer and the CIT(A) held that the shares were purchased with a view to acquiring controlling interest in the company and that the assessee was, therefore, not entitled to deduction under Section 57(iii). The Tribunal, however, allowed the deduction. The assessee did not appear at the hearing of the reference before the High Court. The High Court held: -

"It is clear from a plain reading of above provision that in order to get deduction, the expenditure should be incurred wholly and exclusively for the purpose of making or earning the income from other sources and that it should not be in the nature of capital expenditure. Section 58(1)(a) further provides that no deduction shall be allowed in case the expenditure is in the nature of personal expenses of the assessee. The question which arises in this case is: whether the expenditure incurred for

borrowing money for purchasing shares for acquiring controlling interest in a company can be held to be an expenditure incurred wholly or exclusively for earning income from dividend. There is no dispute in this case that the shares in question were purchased by the assessee for the purpose of acquiring controlling interest in the company and not for earning dividend. That being so, the expenditure incurred by way of interest on the loan taken by the assessee for the said purpose cannot be held to be an expenditure incurred wholly and exclusively for the purpose of earning income by way of dividends. From the nature of transaction, it is clear that the expenditure was not for the purpose of earning income by way of dividends but for the purpose of acquiring controlling interest in the company and, therefore, it would not be allowable as a deduction under section 57(iii) of the Act.

We are supported in our opinion by the decision of the Gujarat High Court in the case of Sarabhai Sons (P.) Ltd. v. CIT, [1993] 201 ITR 464. In that case, it was held that if the dominant purpose for which the expenditure was incurred was not to earn the income, the expenditure incurred in that behalf would fall outside the purview of section 57(iii) of the Act. We are also supported in our above conclusion by the decision of this court in Chinai and Co. Pvt. Ltd. v. CIT, [1994] 206 ITR 616. In that case, there was a dispute in regard to deduction of expenditure under section 37 of the Act. The expenditure was incurred by the assessee in fighting another group of shareholders to protect the investment in the erstwhile managed company. The court held that such an expenditure was not a business expenditure. It was observed that section 37 of the Act dealt with deductions, inter alia, of any expenditure laid out or expended wholly and exclusively for the purposes of business or profession. Such deduction has to be in respect of any expenditure for business which was carried on by the assessee at any time during the previous year. It was held that expenditure incurred in proxy war should not be deducted as business expenditure."

It is important to note that the Court proceeded on the basis that there was no dispute that the shares in question were purchased by the assessee for the purpose of acquiring controlling interest in the company and not for earning dividends. The judgment was based on this fact. As we mentioned earlier, we have proceeded on the basis of the

concession that if shares are purchased with a view to acquiring controlling interest in the company, the assessee is not entitled to a deduction under Section 57(iii). In Commissioner of Income-Tax vs. Amritaben R. Shah (supra), there was a positive finding that the shares were not purchased wholly and exclusively for the purpose of earning income by way of dividends but for acquiring the controlling interest. In the facts and circumstances of this case, it was held that the assessee was not entitled to a deduction under Section 57(iii). Even the judgments referred to in that case proceeded on the basis that the shares were purchased with a view to acquiring a controlling interest in the company and in prosecuting a share-holders' litigation. The judgment does not militate against our view.

35. The questions of law are, therefore, answered in favour of the assessee. The appeal is accordingly allowed and the impugned order of the Tribunal is set aside.

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03.10.2016  
parkash\*

(S. J. VAZIFDAR)  
CHIEF JUSTICE

(DEEPAK SIBAL)  
JUDGE

Note:

Whether ~~non-speaking~~/reasoned ✓  
Whether reportable: YES