

**IN THE HIGH COURT OF KERALA AT ERNAKULAM**

**PRESENT :**

**THE HONOURABLE MR. JUSTICE C.N.RAMACHANDRAN NAIR  
&  
THE HONOURABLE MR. JUSTICE T.R.RAMACHANDRAN NAIR**

**FRIDAY, THE 4TH APRIL 2008 / 15TH CHAITHRA 1930**

**ITA.No. 257 of 2002**

**ITA.593/1996 OF I.T.A.TRIBUNAL,COCHIN BENCH.**

**APPELLANT:**

**THE COMMISSIONER OF INCOME TAX,  
COCHIN.**

**BY ADV. SRI.P.K.R.MENON(SR.),SR.COUNSEL.  
SRI.GEORGE K. GEORGE, SC.**

**RESPONDENT:**

**M/S. MUTHOOT M. GEORGE BANKERS,  
BANERJEE ROAD, ERNAKULAM.**

**BY ADV. SRI.P.BALACHANDRAN,  
ADV. SMT.PREETHA S.NAIR.**

**THIS INCOME TAX APPEAL HAVING BEEN FINALLY HEARD  
ON 25/03/2008, THE COURT ON 04/04/08 DELIVERED  
THE FOLLOWING:**

**C.N. Ramachandran Nair &  
T.R. Ramachandran Nair, JJ.**

-----  
**I.T.A.No.257 of 2002**  
-----

**Dated this the 4<sup>th</sup> day of April, 2008.**

### **JUDGMENT**

T.R. Ramachandran Nair, J.

Revenue is the appellant. The challenge is against the order passed by the Income Tax Appellate Tribunal in I.T.A.No.593/1996.

2. The assessment year is 1989-90. The assessee is a firm engaged in the business of money lending. The assessment was completed under Section 143(3) of the Income Tax Act fixing a total income of Rs.7,45,410/-. While computing the total income, the assessing officer disallowed a sum of Rs.5,15,000/- under Section 40A(3) of the Act which represents interest paid in cash in favour of the minor daughter of a partner. In appeal, the Commissioner of Income Tax (Appeals) took the view in favour of the assessee and accordingly allowed the appeal. The Tribunal after agreeing with the view taken by the Commissioner of Income Tax (Appeals), dismissed the appeal filed by the Revenue.

3. We heard Shri P.K.R. Menon, learned Senior Counsel for the Revenue and Shri P. Balachandran, learned Senior Counsel appearing for the assessee. Learned Standing Counsel for the Revenue contended that

it is actually a case where the relationship of the parties and the manner in which the father of the minor was doing the activities, will justify the view taken by the assessing officer. A reading of the assessment order shows that during the year the assessee had paid an interest of Rs.19,48,990/- on the deposits accepted by it. Out of this, an amount of Rs.5,15,000/- has been paid to one Ms. Susan M. Jacob, who is the minor daughter of Mr. George Jacob, one of the partners of the firm. This amount of Rs.5,15,000/- is paid for a deposit of Rs.10 Lakhs for 4 months. The explanation offered is that the interest paid includes interest payable for the earlier year also and it was pointed out that the minor had deposited Rs.23,50,000/- in December 1986 for nearly 8 months. In fact, during the relevant year she had deposited an amount of Rs.10 lakhs in November and Rs.2 lakhs in March for which interest as noted above, was paid. The sworn statement given by the father was also referred to by the assessing officer. In fact, he explained that the transactions are with the connected firms only and whenever a firm requires money they approach the minor and she in turn accepts money from other firms which are having excess funds and advance it. It is also revealed from the sworn statement that the interest of Rs.5,15,000/- was received in cash. On the admitted facts, the assessing officer was of the view that the above interest said to be received by the minor from the firm is interest received by

the father for the transactions undertaken by him. It is accordingly held that this payment is hit by the provisions of Section 40(b) of the Act.

4. Apart from the above, the transactions show that there were no exigencies which warranted payment by cash. The amount has been utilised for payment of interest to other partners also. It is revealed from the assessment order that the party is having a bank account and the firms with which she is dealing are also having bank accounts. Therefore, it is clear that none of the conditions stipulated in Rule 6DD are present here. Therefore, the assessing officer was of the view that the expenditure has to be disallowed under Section 40A(3) of the Act.

5. Relying upon the above view taken by the assessing officer, learned Standing Counsel for the Revenue contended that the view taken by the assessing officer is perfectly in order and the Commissioner of Income Tax (Appeals) and the Tribunal have not correctly appreciated the relevant evidence and facts in the light of the provisions of the Act. It is submitted that the relevant evidence has been overlooked by the appellate authority and the Tribunal and therefore, the view taken is so perverse and requires interference.

6. As held by the Supreme Court in **Mc DOWELL & Co. v. CTO** (154 ITR 148) colourable devices cannot be accepted as it will invite

evading of payment of tax. The principle as laid down therein will apply to the facts of this case. The transactions have been performed with a minor who is the daughter of one of the partners. The rate of interest that was being granted by the assessee at the maximum was only 18%. But herein for the four months period for Rs.10 lakhs, the assessee has paid interest to the tune of Rs.5,15,000/-. All these will show that the transactions are of colourable nature and the view taken by the assessing officer is perfectly justified.

7. Section 40A(3) as it stood at the relevant time is in the following terms:

“Where the assessee incurs any expenditure in respect of which payment is made, after such date (not being later than the 31<sup>st</sup> day of March, 1969) as may be specified in this behalf by the Central Government by notification in the Official Gazette, in a sum exceeding ten thousand rupees otherwise than by a crossed cheque drawn on a bank or by a crossed bank draft, such expenditure shall not be allowed as a deduction.”

Herein, going by the above provision, any amount exceeding Rs.10,000/- shall not be allowed as deduction. In the light of the above, the view taken by the assessing officer by disallowing the payment by way of interest, under Section 40A(3) of the Act is perfectly correct. It is clear from the facts and evidence discussed by the assessing officer that the interest received by

the minor from the firm represents the amount actually received by her father from the firm. In that view of the matter, the payment of interest is hit by the provisions of Section 40(b) of the Act, as rightly found by the assessing officer. Section 40(b) as it stood at the relevant time is extracted below:

“(b) In the case of any firm, any payment of interest, salary, bonus, commission or remuneration made by the firm to any partner of the firm.

Explanation 1: Where interest is paid by a firm to any partner of the firm who has also paid interest to the firm, the amount of interest to be disallowed under this clause shall be limited to the amount by which the payment of interest by the firm to the partner exceeds the payment of interest by the partner to the firm.

Explanation 2: Where an individual is a partner in a firm on behalf, or for the benefit, of any other person (such partner and the other person being hereinafter referred to as “partner in a representative capacity” and “person so represented” respectively,--

(i) interest paid by the firm to such individual or by such individual to the firm otherwise than as partner in a representative capacity, shall not be taken into account for the purposes of this clause;

ii) interest paid by the firm to such individual or by such individual to the for, as partner in a representative capacity and interest paid by the firm to the person so represented or by the person so represented to the firm, shall be taken into account for the purposes of this clause.

Explanation 3: Where an individual is a partner in a firm otherwise than as partner in a representative capacity, interest paid by the firm to such individual shall not be taken into account for the purposes of this clause, if such interest is received by him on behalf, or for the benefit of any other person.”

8. In the appeal, the appellate authority took the view that the firm had made cash transactions under exceptional circumstances. It was on this premise that the Commissioner of Income Tax (Appeals) took the view that the provisions of Section 40(A)(3) are not applicable. We are of the view that the said view taken by the Commissioner which stands confirmed by the Tribunal, is totally perverse in the light of the facts and evidence discussed by the assessing officer.

In view of the above, we allow the appeal filed by the Revenue setting aside the orders passed by the Commissioner of Income Tax (Appeals) and the Tribunal and restoring the order passed by the assessing officer.

**(C.N. Ramachandran Nair, Judge.)**

**(T.R. Ramachandran Nair, Judge.)**

**kav/**

C.N. Ramachandran Nair &

T.R. Ramachandran Nair, JJ.

-----  
I.T.ANo.257 of 2002  
-----

JUDGMENT

4<sup>th</sup> April, 2008.