* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Date of decision: 30th November, 2012

\+ ITA 258/2010

COMMISSIONER OF INCOME TAX ..... Appellant

Through: Mr. Kamal Sawhney, Sr. Standing Counsel.

versus

UK BOSE ..... Respondent

Through: Mr. Percy J. Pardiwalla, Sr. Advocate with Mr. Satyen Sethi and Mr. Arta Trana Panda, Advocates.

\+ ITA 546/2010

\+ ITA 942/2010

COMMISSIONER OF INCOME TAX CENTRAL I NEW DELHI ..... Appellant

Through: Mr. Kamal Sawhney, Sr. Standing Counsel.

versus

J B ROY ..... Respondent

Through: Mr. Percy J. Pardiwalla, Sr. Advocate with Mr. Satyen Sethi and Mr. Arta Trana Panda, Advocates.

**CORAM:**
**MR. JUSTICE S. RAVINDRA BHAT**
**MR. JUSTICE R.V. EASWAR**

**R.V. EASWAR,J: (OPEN COURT)**

The common question of law which arises in all the three appeals by the revenue relates to the assessment of the perquisites in the hands of the respective assessees. In ITA No.942/2010 the substantial question of law is as under:-

> "*(i) Whether the Income Tax Appellate Tribunal was correct in law in deleting the addition of ₹7,37,025/- made by the AO on account of perquisites u/s 28(v) of the Act?*

2. In ITA No. 546/2010 the substantial question of law is as under:-

> "*(i) Whether the Income Tax Appellate Tribunal was correct in law in deleting the addition of ₹6,29,366/- made by the AO on account of perquisites u/s 28(v) of the Act?*

3. In ITA No.258/2010 the substantial question of law is as under:-

> "*(i) Whether the ITAT was correct in law in deleting the addition made by the Assessing Officer on account of perquisite value in the hands of assessee?*

4. We may first take up ITA No.258/2010, in which the assessee is one U.K.Bose. He at the relevant time was an employee of M/s Sahara Airlines Ltd. In respect of the assessment year 2000-01 the assessing officer noticed in the course of the assessment proceedings that the assessee was provided with several perquisites by his employer. They were in the shape of credit card expenses, club partnership expenses, expenses on domestic servants, expenses on security guard, chauffer driven car, telephone/cell phone expenses, electricity expenses etc. He considered these expenses incurred by the employer-company as perquisites arising out of employment and taxable under

Section 17 of the Act. He accordingly brought the aggregate amount of ₹2,94,843/- to tax as under:-

| | | |
|---|---|---|
| *Credit Card expenses* | *6* | *86,363* |
| *Club Membership* | *7* | *20,000* |
| *Domestic Servant* | *8* | *24,000* |
| *Security guards* | *9* | *2,880* |
| *Chauffeur Driven car* | *10* | *90,000* |
| *Telephone/ cell expenses* | *11* | *50,000* |
| *Electricity Expenses* | *12* | *12,000* |
| *Conveyance* | *13* | *9,600* |

5. On appeal the CIT(Appeals), following his earlier orders, deleted the entire amount of ₹2,94,843/- on the ground that the addition was made on hypothetical and estimated basis. The Revenue carried the matter in appeal before the Income Tax Appellate Tribunal ('Tribunal' for short) in ITA No.1502/Del/2008. The Tribunal accepted the ground and noted that in the appeal of the Revenue for the assessment year 1998-99 in ITA No.1500/Del/2008, it had by order dated 17th April, 2009 held that the assessee was not provided with any accommodation by his employer, that no furniture or security guards or cooks were provided to him and that the telephone was provided by the firm by name M/s Sahara India Mass Communication, in which the assessee was a partner and that considering all these circumstances the CIT(Appeals) had rightly deleted the perquisites brought to assessment by the assessing officer. Following its earlier order, the Tribunal took the same view holding as follows:-

> *"In the present case we find that the additions in respect of perquisite value were towards electricity expenses, rent free*

*accommodation, value of domestic servant, security guard, telephone at residence, chauffeur driven car, other amenities, club membership and in respect of foreign travel undertaken by the assessee. However, we find that all these additions were made without finding that the company has incurred such expenses by way of providing perquisite to the assessee and not incurred by the company in the course of carrying on business. The additions were made on estimate basis. Since the facts are identical in the case of the assessee for Assessment Year 1998-99, we do not find any infirmity in the order of the learned CIT (A)."*

6. We have considered the matter in the light of the rival contentions. The Tribunal has recorded a finding of fact that the company which employed the assessee did not incur any such expenses for providing these perquisites to the assessee and that the additions were made only on estimate. There is no material before us to show that the finding of fact recorded by the Tribunal is contrary to the record or is untenable. We accordingly answer the substantial question of law in the affirmative, in favour of the assessee and against the revenue.

7. So far as the ITA No.942 & 546/2010 are concerned, they relate to the assessee by name J.B. Roy, for the assessment years 2001-02 and 2000-01 respectively. In respect of these years, the assessee was a partner of M/s Sahara India and director in various companies of Sahara Group. He was drawing salary from M/s Sahara India Mass Communication. In the assessments the assessing officer added the perquisite value on account of provision of security guards and gardener to the assessee in the amount of ₹7,37,025/- for the assessment year 2001-02. The value of perquisite on account of provision of chauffer driven car was taken at ₹2 lacs. The other perquisites assessed were

₹2,11,500/- for domestic servants, ₹5,000/- for gas and water charges and ₹1,24,069/- for telephone expenses. The value of perquisites on account of security guards and gardener was assessed under Section 2(24)(iv) and the perquisites aggregating to ₹5,40,569/- was assessed under Section 28(v) since these were provided by M/s Sahara India Finance Corporation which was the assessee's employer.

8. On appeal the CIT (Appeals) deleted the addition on account of perquisites whose order was confirmed by the Tribunal.

9. In respect of the assessment year 2000-01, the position is the same except for variations in the amount of perquisites added.

10. We have considered the facts in the light of the arguments addressed before us. The findings recorded by the Tribunal are findings of fact. So far as the salaries paid to security guards, servants and gardener are concerned, they have been found debited to the account of the assessee in the books of the firm M/s Sahara India and, therefore, there is no question of perquisites. Similarly, it has been found by the Tribunal that the rent was paid by the firm in respect of the property which was not owned by the firm and, therefore, there was no concession in the matter of either rent or furniture and fixtures. Considering these findings of facts, we see no reason to interfere with the orders of the Tribunal in these two appeals so far as the issue of perquisites is concerned. Accordingly the first substantial questions of law in these two appeals are answered in the affirmative, in favour of the assessee and against the Revenue.

11. The second substantial question of law in these two appeals relating to J.B.Roy is:-

> "(ii) *Whether the Income Tax Appellate Tribunal was correct in law in allowing deduction of ₹3,84,000/- to the assessee under Section 10(13A) of the Act for the assessment year 2001-02*?"

12. In respect of the other assessee, question of law is the same but the amount involved is ₹2,31,000/-. In the returns the assessee had claimed deduction under Section 10(13A) on the basis of the rent paid by him which has been debited from his salary directly. This Section exempts any special allowances specifically granted to an assessee by his employer to meet expenditure actually incurred on payment of rent for residential accommodation occupied by the assessee, to such extent as may be prescribed, having regard to the area in which the accommodation is situated and other relevant considerations. Rule 2A of the Income Tax Rules prescribes the quantum of exemption available. The reason why the assessing officer disallowed the claim for exemption is that he considered the salary received from M/s Sahara India Mass Communication not under the head "salary" but under the head "income from other sources". The reasoning of the assessing Officer as contained in the assessment order for the assessment year 2001-02 is as under:-

> *"8. The assessee has disclosed income from salary received from M/s. Sahara India Mass Communication amounting to ₹35,16,000/-. The assessee has claimed deduction u/s 10(13A) at ₹3,84,000/- on the basis of rent paid by him which has been debited from his salary directly.*

*8.1 It is noted that the promoters (Sri Subrato Roy, the assessee and Sri O.P. Srivasata) have devised a system by which they are drawing salary from some concern, perquisite from another, etc. The whole system works in a fashion that their personal/ family needs are being taken care of by the various concerns without their showing the value as income (partly or wholly) and paying tax on it. It is evident that this privileged treatment is received by them by virtue of their overall position in the group and particular position in the respective firms/ companies in which they are partners/ directors. Here it is also to point out that last year his employer has given him a gross salary of ₹16,89,000/- but during the year under consideration the salary of the assessee has increased more than double without any special reason, or gain to company. This also proves that the assessee is enjoying the benefit of his position in the group and drawing the salary what he want. In view of the aforesaid, the income of ₹35,16,000/- disclosed by the assessee from salary is being treated as income within the meaning of section 2(24)(iv) and assessed under the head 'income from other sources'. The claim of exemption u/s 10(13A) is, accordingly, not being allowed."*

13. On appeal the CIT (Appeals) following his earlier orders directed the assessing officer to allow the exemption. The revenue carried the matter in appeal to the Tribunal. The Tribunal following its order for the assessment year 1999-2000 affirmed the decision of the CIT (Appeals).

14. We have considered the issue in the light of the rival contentions. The ground on which the claim for exemption under Section 10(13A) was rejected by the assessing officer was that the salary receipts by the assessee from M/s Sahara India Mass Communication cannot be assessed under the head "salary", but should be assessed under the head "income from other sources". The assessing officer has however not brought any material to show that the

relationship between the M/s Sahara India Mass Communication and the assessee was not that of a master and servant. He has referred to some extraneous material to hold that the salary receipt should be assessed as income from other sources. Unless there is material to show that there was no employer-employee relationship, the proper head of income to be applied is that of "salary". Since this is not the case of the assessing officer, we are of the view that the Tribunal was right in holding that the assessee was entitled to the exemption under Section 10(13A). In this view of the matter, we answer the second substantial question of law in these two appeals in the affirmative, in favour of the assessee and against the revenue.

15. That leaves us with the second substantial question of law in ITA No.258/2010 which is as under: -

> *(ii) Whether the ITAT was correct in law in deleting the addition of ₹10,12,529/- made by the assessing officer on account of interest paid by the assessee on loan taken for purchase of an exempted asset?"*

We may notice the facts giving rise to the question. The assessee received interest of ₹17,87,426/- from Sahara India Commercial Corporation Ltd. (SICCL) against which it claimed deduction of ₹10,12,524/-, being interest paid to the same entity i.e. SICCL and declared the net interest of ₹7,74,897/- as his income. The income was shown under the head "income from other sources". The assessing officer called upon the assessee to explain the claim for deduction of the interest. In response thereto the assessee wrote a letter on 11.10.2002 as follows:

"*During the year assessee has **received interest from Sahara India Commercial Corporation Limited in respect of land sold to them** against which the **sales proceeds were received late** and on the other hand has **also paid interest on the loan obtained earlier for the purchase of the said land.** The difference of the same has also been offered for the assessment in the revised return. The assessee was under wrong impression that since the **sale of land was not taxable receipt in the hand of the assessee**, it was presumed that the interest element also was not taxable and obtaining proper legal advise, the same is being offered for assessment…..*"

16. After considering the reply, the assessing officer called upon the assessee to explain why the interest paid to SICCL should not be disallowed. The assessee replied as under:

"*…..As regards interest payment to SICCL, the same is a fully allowable deduction as it directly relates to the interest received by the assessee on **late remittance of the sale proceeds of lands**. If the sale proceeds would have been received in time, the assessee would have paid off the loan taken for the purpose of investment, but there was late receipt of sale proceeds on which interest has been received by the assessee which is also offered for assessment and against the same interest paid on loan is claimed as a deduction as the transaction is interrelated with each other. Under the circumstances interest payment is allowable deduction in the hands of the assessee on the same footing on which interest received by the assessee is taxable…..*"

It would appear that the interest liability had been capitalised towards the actual cost of the land. Therefore, the assessing officer sought clarification as to how the capitalised interest can be allowed to be adjusted against the interest received. The assessee by letter dated 10.2.2003 clarified the issue as follows:-

"……*No doubt, the interest which was payable on the loan for the purchase of the land has been capitalised the cost of the land because it was a capital asset in the hands of the assessee but your honour will appreciate that the interest which is being set off by the assessee is* ***subsequent to the date of sale of the land****.*

*We have already explained to your honour in our earlier written submission that the interest payment received from SICCL is on account of* ***late remittance of the sale proceeds*** *of land by them to the assessee. In turn, the assessee could square off his loan taken for the purchase of land at a later date and, therefore, the assessee had to pay interest also for the period subsequent form the* ***date of sale till the date of actual payment****.*

*On the date of sale of the land, the treatment of capitalising interest towards the capital asset has ended as the capital asset remains no more in existence.*

*What was due now was the sale proceeds against the land. If the sale proceeds would have been received immediately, the assessee would have paid off loan* ***taken for the purchase of the investment to be paid by the assessee****. But since the sale proceeds has been remitted to the assessee late and interest has been received by the assessee on such late remittance, the interest which has been paid by the assessee on the loan from the date of the sale till the date of repayment of the loan is an interrelated transaction with each other and, therefore, the interest which has been paid is fully allowable deduction in the hands of the assessee……*"

17. The assessing officer was of the view that there was no provision in the Act to allow the interest paid against the interest received by the assessee. He also examined the provisions of Section 57(iii) of the Act and held that the interest liability cannot be claimed as deduction under those provisions. He referred to the judgment of the Supreme Court in *CIT vs. Dr. V.P.Gopinathan*

*(2001) 248 ITR 449* and held that the gross interest of ₹17,87,426/- was assessable to tax and the same was brought to charge under the head "income from other sources".

18. On appeal the CIT (Appeals) agreed with the assessee and directed the assessing officer to allow the interest payment of ₹10,12,529/- and to assess only the balance of ₹7,74,897/-. His reasoning was like this. The moment the assessee entered into an agreement of sale in respect of the agricultural land, he had a right to receive the sale proceeds from the buyer of the land, who was none other than the person from whom the assessee borrowed monies on interest for acquiring the land. On the one hand the assessee had the right to receive the monies from SICCL and on the other, he had the liability to pay interest to SICCL. According to the CIT (Appeals) the two transactions were interlinked and had a direct nexus with each other. If the assessee had received the sale proceeds immediately on transfer of the land to SICCL, he would have been in a position to also clear his loan to SICCL and thus there would have been no liability to pay or right to receive the interest. Since both the transactions were closely related to each other, the CIT(Appeals) was of the view that the interest received and the interest paid should be set off against each other and only the balance, being the excess interest of ₹7,74,897/-, can be brought to tax under the head "income from other sources". He thus allowed the assessee's appeal on this point.

19. The Revenue carried the matter in appeal to the Tribunal in ITA No.1502/Del/2008. The Tribunal was inclined to view both the transactions as interconnected. This is what the Tribunal held:-

*"10. We have considered the rival submissions. The interest paid by the assessee was initially in respect of loan taken for purchase of agricultural land. Thus till the land was held by the assessee, the interest there on is not allowable as the same is in respect of agricultural land which is not a capital asset and no capital gain is chargeable in this respect. However, the interest payable after the land was sold cannot be considered as for acquisition of any capital asset. The same was in the nature of amount borrowed. Since the assessee did not receive the sale price of land sold, the assessee could not repay the debt. On the amount receivable from the person to whom the land was sold, the assessee had charged interest and offered the same for taxation. Thus the amount borrowed can now be attributed to the loan for financing the amount receivable. In such a situation there is a direct nexus between the amount borrowed and the amount advanced. In respect of amount advanced the assessee was to receive the interest. Such interest could not have been received, had the assessee not borrowed. Therefore, the interest payable on the borowal being in respect of amount advanced on which the interest is received. The assessee was rightly held to be eligible for deduction of such interest paid. Accordingly ground No.3 in appeals for Assessment Year 2000-01 and 2001-02 fails."*

20. It is the correctness of the above decision of the Tribunal that is called in question by the Revenue. Strong reliance was placed on the judgment of the Supreme Court in *CIT vs. Dr. V.P.Gopinathan* (supra). It is submitted that Section 57(iii) cannot apply at all and the assessee cannot claim a deduction for the interest paid, since it was not paid for the purpose of making or earning the interest received. Relying on the judgment of the Supreme Court (supra) it is contended that even a set off on the principle of real income or any other principle deduction of the interest paid cannot be granted since the transactions

giving rise to the interest receipt and the interest payment are different transactions having no commonality or connection.

21. The contention of the assessee is that the principle of netting or set off would apply since both the transactions are with the same person i.e. SICCL; it is pointed out that, had the SICCL paid the purchase price in time, the assessee could have used the same to repay the borrowing from SICCL which it was deprived of. The interest liability arose only because of the delay in SICCL paying the purchase price and that way the transactions giving rise to the interest receipt and the interest payment was one and the same. This, according to Mr. Pardiwala, the learned counsel for the assessee, affords the nexus or close link between the interest receipt and the interest payment justifying the adjustment or set off.

22. In support of the submissions, Mr.Pardiwala has placed strong reliance on the judgment of the Supreme Court in *Keshavji Ravji and Co. vs. Commissioner of Income-tax (1990) 183 ITR page 1*. Reference has also been made to another Supreme Court judgment in *Associated Capsules Pvt. Ltd. v. ACIT*, (2012) 343 ITR 89 and a judgment of a Division Bench of this Court in *CIT v. Shri Ram Honda Power Equip, (2007) 289 ITR 475*.

23. It would prima facie appear that the judgment of the Supreme Court in *CIT vs. Dr.V.P.Gopinathan* (Supra) is against the claim of the assessee but a closer look at the facts shows that the judgment of the Supreme Court in *Keshavji Ravji & Co. vs. CIT* (Supra) is closer to the assessee's case on principle. In the former, the assessee had placed monies in a fixed deposit with the bank. On the security of the fixed deposit, he took a loan. The interest

received on the fixed deposit and the interest paid on the loan were sought to be adjusted against each other and only the net interest was offered for tax. The assessee did not put his case under Section 57(iii), but relied on the principle of mutual dealings and real income theory. The Supreme Court rejected the claim, holding as under:-

> *"It was not disputed, as it could not be, that if the assessee had taken a loan from another bank and paid interest thereon his real income would not diminish to the extent thereof. The only question then is : does it make any difference that he took the loan from the same bank in which he had placed the fixed deposit. There is no difference in the eye of the law. The interest that the assessee received from the bank was income in his hands. It could stand diminished only if there was a provision in law which permits such diminution. There is none, and, therefore, the amount paid by the assessee as interest on the loan that he took from the bank did not reduce his income by way of interest on the fixed deposit placed by him in the bank."*

The judgment of the Supreme Court in *Keshavji Ravji* (Supra) is earlier in point of time and was also rendered by a Bench of equal strength i.e. three Judges. In *Keshavji Ravji* (supra) the provisions of Section 40(b) of the Act came up for consideration. Under this provision, any interest paid by the firm to its partner was to be disallowed and added back to the income of the firm. A question arose as to what should be the quantum of the interest to be disallowed, when the firm is both in receipt of interest from the partner on monies advanced to him and also pays interest to him. According to the Revenue, the receipt of interest from the partner had to be ignored and the amount paid by the firm to the partner had to be disallowed; whereas according to the assessee, both the amounts should be netted and only the excess interest paid, if any, over and above the interest received by the firm, could be

disallowed. The view of the CBDT in Circular No.33D of 1965 was in accord with the view of the assessee. The Supreme Court was, inter alia, dealing with the argument of the assessee that the interest payable by the firm to the partner and by the partner to the firm is of the same nature and both being integral parts of a method adopted by the partners for adjusting the division of the profit, both payments partake of the same character and in that sense they should be set off against each other and only the net payment should be disallowed. The Supreme Court opined that this general principle, if found to be departed from under the Income Tax law either expressly or by necessary implication, cannot be given effect to; but if there is no statutory departure, the general principle operating under the general law determining the nature of the legal relationship between the parties can be applied in the interpretation of the provisions of the Act. The position was ultimately summed up as follows:-

> "*How do these principles operate on the present controversy? It appears to us that, if, in substance, the interest paid by the firm to a partner and the interest, in turn, received from the partner are mere expressions of the applications of the funds or profits of the partnership and which, having regard to the community of interest of the partners, are mere variations of the method of adjustment of the profits, there should be no impediment in treating them as part of the same transaction if, otherwise, in general law, they admit of being so treated. The provisions of section 40(b) do not exclude or prohibit such an approach. If, instead of the transactions being reflected in two separate or distinct accounts in the books of the partnership, they were in one account, the quantum of interest paid by the firm to the partner would, to the extent of the drawings of the partner, stand attenuated. The mere fact that the transactions are split into or spread over two or more accounts should not, by itself, make any*

*difference if, otherwise, the substance of the transaction is the same. One of the relevant tests would be to see whether the funds on which interest is paid or received partake of the same character.*"

Having said so, the Supreme Court referred to the principle of 'set off' statutorily recognized in bankruptcy proceedings under Section 46 of the Provincial Insolvency Act, 1920 and Section 529 of the Companies Act, 1956 which provides for "mutual credit" to avoid injustice which would otherwise be caused by compelling a creditor to pay the official assignee the full amount of debt due from him to the insolvent while the creditor would receive only a small dividend on the debt due from the insolvent to him under "*pari passu*" payment. The concept of set off was held applicable even under the Income Tax Law which identifies the firm as a distinct entity and unit of assessment, having regard to mutuality concept implicit in the dealings between the partners and the firm.

24. The netting principle was adopted by a Division Bench of this Court in *CIT vs. Shri Ram Honda* (supra). That was a case concerning Section 80HHC which provides for a deduction from export profits. Explanation (baa) provided for exclusion of certain income which had nothing to do with the export profit and one such item of income was interest. This Court held that the interest which had to be excluded from the business profits was not the gross amount of interest, but only the net interest after adjusting the expenditure incurred by the assessee to earn such interest. There was reference made to the judgment of the Supreme Court in *Keshavji Ravji* (Supra) and it was observed by this Court in paragraph 51 of the judgment that the underlying principle of netting would get attracted as no prudent business man would allow taxation of interest income

without the expenditure incurred for earning the same being taken into account. There is also the overriding principle in tax law that it is not the gross receipt that falls to be assessed but it is only the net income, after all the expenditure to earn the income is deducted, that can be assessed to tax. Strictly speaking, in the present case it is not a question of any deduction being allowed from the interest receipt; it is really a question of adjusting or setting off both the interest received and the interest paid, since both have close link or nexus with each other. The Tribunal has recorded a finding that the agricultural land was sold by the assessee in the month of February, 1999 to SICCL. From the date of sale of the land till the remittance of the sale proceeds the assessee was to pay interest of ₹10,12,529/- on the loan which he had taken for purchase of the land. It is in respect of the same period that he was entitled to interest income of ₹17,18,426/- from SICCL. Had there been no delay by SICCL in the remittance of the sale proceeds, there would have been no interest liability. The right to receive the interest and the liability to pay interest arose in respect of the same period and out of the same event i.e. non-payment of the sale proceeds in time. The delay in payment of the sale proceeds and the delay in repayment of the borrowing are both intertwined; one gives rise to interest income and the other gives rise to interest liability. We are of the view that this affords sufficient nexus between the two so as to justify the applicability of the principle of netting.

25. For the aforesaid reasons, we affirm the decision of the Tribunal on this point and answer the substantial question of law in the affirmative, in favour of the assessee and against the Revenue.

26. In the result all the appeals filed by the Revenue are dismissed. There shall be no order as to costs.

**R.V.EASWAR, J**

**S. RAVINDRA BHAT, J**

**NOVEMBER 30, 2012**
**Bisht**