

A DEVI CINE PROJECTOR MANUFACTURING
 CO., ETC. ETC.

v.

COMMISSIONER OF INCOME TAX

FEBRUARY 5, 1990

B [M.N. VENKATACHALIAH, N.D. OJHA AND
 J.S. VERMA, JJ.]

C *Income Tax Act, 1961: Section 40(b)—Disallowance of interest—
Firm paying interest to partner—Partner also paying interest to firm on
borrowing from firm—Whether such interest to be confined only to net
amount after setting off interest paid by partner.*

D *Constitution of India, 1950: Article 136—Special Leave Petitions
filed against High Court's rejection of assessee's applications under Sec-
tion 256(2) of the Income Tax Act, 1961—In view of settled position on
point of law involved and to avoid time consuming procedure, Special
Leave Petitions treated as arising out of appellate orders of Tribunal
and matter remitted to Tribunal for disposal afresh in the light of pro-
nouncement of Court.*

E The Income Tax Appellate Tribunal in appeals preferred before it
by the revenue held that the entirety of interest paid by a firm to its
partner was disallowable under Section 40(b) of the Income Tax Act without
reference to the interest that might, in turn, have been paid by the partner
to the firm on his borrowings. On appellants-assessee's application
under Section 256(1) of the Act, the Tribunal declined to state a case and refer a question of law for the opinion of the High Court. The
F appellants-assessee's then moved Tax case petitions under Section 256(2)
of the Act before the High Court. The High Court rejected the applica-
tions on the view that there was no referable question of law arising out
of the appellate order of the Tribunal having regard to its earlier deci-
sion in *C.I.T. v. O.M.S.S. Sankaralinga Nadar & Co.*, 147 ITR 332, on
which the Tribunal had relied. The appellants-assessee's filed special
G leave petitions in this Court.

Treating the special leave petitions as directed against the main
appellate order of the Tribunal, and allowing the appeals, this Court,

H HELD: It is now settled by the pronouncement of this Court in
Keshavji Ravji & Co. v. C.I.T., [1990] 1 S.C.R. 243 that where two or

more transactions on which interest is paid to or received from the partner by the firm are shown to have the element of mutuality and are referable to the funds of the partnership as such, Section 40(b) should not be so construed as to exclude in quantifying the interest, if any, paid to a partner by the firm in excess of what was received from the partner. [270F] **A**

Keshavji Ravji & Co., [1990] 1 S.C.R. 243, followed. **B**

C.I.T. v. O.M.S.S. Sankaralinga Nadar & Co., 147 ITR 332, over-ruled.

In the instant case, the appeals were directed against the High Court's orders rejecting the assessee's applications under Section 256(2) of the Act. However, remitting the cases to the High Court in the normal course for necessary action would be an idle, time-consuming and avoidable formality. Further, as the position is settled on the point raised, interests of justice would be served by treating the appeals as directed against the main appellate orders of the Tribunal and remitting the cases to the Tribunal for disposal. [270B; 271A-B] **C** **D**

Accordingly, the orders of the Tribunal and of the High Court are set aside, and the appeals remitted to the Tribunal for disposal afresh on the extent of disallowance of interest under Section 40(b) of the Act in the light of pronouncement of this Court in *Keshavji Ravji & Co. v. C.I.T.*, [1990] 1 S.C.R.243. [271E-F] **E**

CIVIL APPELLATE JURISDICTION: Civil Appeal Nos. 1185 to 1188 (NT) of 1990.

From the Judgments and Orders dated 7.11.1985, 12.8.85, 6.2.85 and 24.7.86 of Madras High Court in T.C.P. Nos. 739/85, 313/85, 260/84 and 42/86. **F**

T.A. Ramachandran and Mrs. Janaki Ramachandran for the Appellants. **G**

S.C. Manchanda, B.B. Ahuja and Ms. A. Subhashini for the Respondent.

The Judgment of the Court was delivered by

VENKATACHALIAH, J. These four petitions for grant of **H**

A special leave arise out of the orders of the High Court of Judicature at Madras in the corresponding four Tax Case Petitions rejecting the assessee's applications under Section 256(2) of the Income-tax Act, 1961 and the reference of a question of law whether the disallowance under Section 40(b) of the Income Tax Act, 1961 (Act) of the interest paid by the firm to its partner should be the gross amount of such interest or should be confined to the net-amount after setting-off the interest, in turn, paid by the partner to the firm on his borrowings from the firm.

2. In each of these cases the Income Tax Appellate Tribunal had, in substance, held that what was disallowable was the entirety of the interest paid by the firm to the partner without reference to any interest that may, in turn, have been paid by the partner to the firm. The Tribunal in the appeals preferred by the Revenue before it, allowed the appeals and reversed the view to the contrary taken in favour of the assesseees by the first-appellate authority. The Tribunal also declined to state a case and refer a question of law under Section 256(1) of the Act to the High Court; whereupon the assesseees moved the aforesaid Tax Case Petitions before the High Court under Section 256(2). The High Court rejected these applications on the view that there was no referable question of law arising out of the appellate orders of the Tribunal, having regard to the earlier pronouncement of the High Court in *C.I.T. v. O.M.S.S. Sankaralinga Nadar & Co.*, 147 ITR 332 on which the Tribunal had relied.

3. The correctness of the decision of the High Court in the said *Sankaralinga Nadar's* case has come to be examined by this Court in *Keshavji Ravji & Co. v. C.I.T.*, [1990] 1 S.C.R. 243 this Court has taken a view in the light of which *Sankaralinga Nadar & Co.'s* case cannot be held to have laid down the law correctly in all respects. The pronouncement of this Court in the said *Keshavji Ravji & Co's* case (supra) covers the point raised in these Special Leave Petitions.

4. However, as the present special leave petitions arise out of the orders of the High Court rejecting the Tax Case Petitions under Section 256(2) of the Act, we should, in the normal course, grant special leave, register the corresponding civil-appeals and after setting-aside the orders of the High Court remit the corresponding Tax Case Petitions to the High Court with a direction to allow petitions and to direct the Income Tax Appellate Tribunal to state a case and refer a question of law for the opinion of the High Court and thereafter, to

dispose-of the references in the light of the pronouncement of this Court in the said *Keshavji Ravji & Co.*'s case. This procedure would, indeed, be an idle, time-consuming and wholly avoidable formality in the circumstances of the present cases. As the position is now settled, we are of the opinion that interests of justice would be served by treating the present Special Leave Petitions as directed against and arising from the main Appellate Orders of the Income Tax Appellate Tribunal, Madras, and after granting Special Leave, set-aside that part of the appellate orders as pertain to the extent of disallowance of the interest under Section 40(b) of the Act and direct the Tribunal to dispose of the appeals on the point afresh in the light of the aforesaid pronouncement of this Court.

5. These petitions are, therefore, treated as directed against the main Appellate Judgments dated 9.3.1984 in ITA 1521/Mds/1982; 29.2.84 in ITA No. 898/Mds/1982; 30.8.1983 in ITA 1520/Mds/82 and 22.2.1984 in ITA 1848/Mds/83 of the Income Tax Appellate Tribunal, Madras and Special Leave granted.

The orders of the Tribunal made under Section 256(1) of the Act in each of these cases as well as the orders of the High Court in Tax Case Petition 739 of 1985, 313 of 1985, 260 of 1984 and 42 of 1986 are set-aside.

Further, the appellate orders of the Income-tax Appellate Tribunal, in so far as they pertain to the extent of disallowance of interest under Section 40(b) of the Act, are set aside and the said appeals remitted to the Tribunal for a fresh disposal of the appeals on the point in the light of the pronouncement in *Keshavji Ravji & Co.*'s case.

6. There will, however, be no order as to costs.

N.P.V.

Appeals allowed.