

DEPUTY COMMISSIONER OF INCOME TAX, CHENNAI

v.

T. JAYACHANDRAN

(Civil Appeal No. 4341 of 2018)

APRIL 24, 2018

[R. K. AGRAWAL AND NAVIN SINHA, JJ.]

Income Tax Act, 1961 – Additional interest – Respondent, an approved broker for Indian Bank – Case of revenue was that Indian Bank raised its funds by way of receiving amount from the PSU and making fixed term deposit on higher rate of interest – In order to pay higher interest to these PSUs, the bank requested the respondent to purchase securities on its behalf – Thereafter, respondent purchased securities at a particular rate quoted by the bank and was paid commission in respect of transactions done on behalf of Indian Bank – Under instructions from Indian Bank, a portion of amount realised from the security transactions carried on behalf of Indian Bank was paid by way of additional interest to certain PSUs on the deposits made with the Indian Bank – Assessing officer made demand from the respondent with regard to the sum payable to the PSUs holding that the respondent did not act as a broker in the transactions carried out for Indian Bank rather as an independent dealer and that there was no overriding title in favour of PSUs with regard to the additional amount earned out of the securities transactions and the said amount is liable to be assessed as the income of the respondent – Held: Whether the alleged interest payable to the PSUs can be assessed as an income of the respondent depends on the determination of true nature of relationship between the Indian Bank and the respondent with regard to the transactions in question and the capacity in which he held the amount – The normal settlement process in Government securities is that during transaction banks make payments and deliver the securities directly to each other – The broker's only function is to bring the buyer and seller together and help them to negotiate the terms for which he earns a commission from both the parties – He does not handle either cash or securities – The

- A *evidence led by bank officials show that the price of securities itself were fixed by the bank authorities and as per their directions the respondent had purchased the securities at the market price and the differential amount was directed to be used for taking demand drafts from the bank itself for paying additional interest to the PSUs which is sufficient to prove the fact that the respondent*
- B *acted as a broker to the Bank and, hence, the additional interest payable to the PSUs could not be held to be his property or income.*

Disposing of the appeals, the Court

- C **HELD: 1. Whether the alleged interest payable to the PSUs can be assessed as an income of the Respondent depends on the determination of true nature of relationship between the Indian Bank and the Respondent with regard to the transactions in question and the capacity in which he held the amount of Rs. 14,73,91,000/-. The normal settlement process in Government**
- D **securities is that during transaction banks make payments and deliver the securities directly to each other. The broker's only function is to bring the buyer and seller together and help them to negotiate the terms for which he earns a commission from both the parties. He does not handle either cash or securities.**
- E **In this respect, the broker functions like the broker in the inter bank foreign exchange market. The conduct of the Respondent in the transaction in question cannot be termed to be strictly within the normal course of business and the irregularities can be noticed from the manner in which the whole transactions were conducted. However, the same cannot be basis for holding the**
- F **Respondent liable for tax with regard to the sum in question and what is required to be seen is whether there accrued any real income to the Respondent or not. It is required to be seen in what capacity the Respondent held the said amount-independently or on behalf of the Indian Bank. [Paras 10, 11] [625-E-G; 626-A]**
- G **2. The relationship between the Indian Bank and the Respondent is very much clear by the evidence led during the criminal proceedings. The Executive Director of the Bank has specifically spoken about the role of the Respondent as a broker**
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specifically engaged by the Bank for the purchase of securities and that the Bank has included the interest money too in the consideration paid, for the purpose of taking demand drafts in favour of PSUs. Further, the evidence led by other bank officials points out that the price of securities itself were fixed by the bank authorities and as per their directions the Respondent had purchased the securities at the market price and the differential amount was directed to be used for taking demand drafts from the bank itself for paying additional interest to the PSUs. The conduct of the parties, as is recorded in the criminal proceedings showing the receipt of amount by the broker, the purpose of receipt and the demand drafts taken by the broker at the instance of the bank were sufficient to prove the fact that the Respondent acted as a broker to the Bank and, hence, the additional interest payable to the PSUs could not be held to be his property or income. [Para 12] [626-F-H; 627-A-B]

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 4341 of 2018. D

From the Order dated 29.10.2012 of the High Court of Judicature at Madras in TC No. 368 of 2005

WITH E

Civil Appeal Nos. 4342-4243, 4349-4350, 4344, 4346-4348, 4351, 4352, 4353, 4354, 4355, 4345, 4350 and 4357 of 2018.

Arijit Prasad, Ms. Sadhana Sandhu (for Mrs. Anil Katiyar) Advs. for the Appellant. F

Biswajit Bhattacharya, Arvind P. Datar, Mukul Rohatgi, Sr. Advs., Elam Bharathi, Sumit Kumar, Pratap Venugopal, Ms. Surekha Raman, Anuj Sarma, Ms. Niharika, Ms. Kanika Kalaiyaran (for M/s K.J. John & Co.), Preetesh Kapoor, Sanjay Kapur, Ms. Megha Karnwal, Ms. Shubhra Kapur, Sanjay Kapur, Ms. Vanita Bhargava, Ajay Bhargava, Roy O. John (for M/s. Khaitan and Co.), Advs. for the Respondent. G

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A The Judgment of the Court was delivered by

R.K. AGRAWAL, J. 1. Leave granted.

2. The present appeal has been filed against the impugned judgment and order dated 29.10.2012 passed by the High Court of Judicature at Madras in Tax Case (Appeal) No. 368 of 2005 wherein the Division
B Bench of the High Court allowed the appeal filed by the respondent by absolving the additional tax liability imposed by the Assessing Officer, vide order dated 25.01.1996.

3. Brief facts:-

C (a) The Respondent - an individual and the proprietor of M/s Chandrakala and Company, is a stock broker registered with the Madras Stock Exchange. He is stated to be an approved broker of the Indian Bank. The assessment years under consideration herein are 1991-92, 1992-93 and 1993-94 respectively. During all these relevant assessment years the Respondent acted as a broker to the Indian Bank in purchase
D of the securities from different financial institutions.

(b) It is the case of the Revenue that the Indian Bank, in order to save itself from being charged unusually high rate of interest on borrowing money from the market, lured Public Sector Undertaking (PSUs) to make fixed term deposit with it on higher rate of interest. The rate of
E interest offered to the PSUs for making huge term deposits was to the extent of 12.75% of interest on fixed deposits against the approved 8% rate of interest in accordance with the RBI directions.

(c) In order to pay higher interest to the PSUs who made a fixed term deposit with the Indian Bank, the bank requested the Respondent
F to purchase securities on its behalf at a prescribed price which was unusually high but adequate to cover the market price of the securities, brokerage/incidental charges to be levied by the Respondent on these transactions, apart from covering the extra interest payable to the PSUs. The Respondent, on the instructions of Indian Bank, purchased securities
G at a particular rate quoted by the Bank and sold them to Indian Railways Finance Corporation. Bank of Madura was the routing bank through which the securities were purchased and sold to Indian Bank for which Bank of Madura charged service charges. The Respondent was paid commission in respect of transactions done on behalf of Indian Bank. Under instructions from Indian Bank, a portion of the amount realized

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from the security transactions carried on behalf of Indian Bank was paid by way of additional interest to certain Public Sector Undertakings (PSU) on the deposits made with the Indian Bank and out of eight PSUs three has confirmed the receipt of such additional interest through demand drafts. A

(d) The Respondent filed his return of income for the Assessment Year 1991-92 on 01.11.1993 and declared his income at Rs. 4,82,83,620/-. The total income was determined at 4,85,46,120/- vide order dated 30.06.1994. However, later on, the case was taken up for scrutiny and assessment was framed under Sec 143(3) of the Income Tax Act, 1961 (in short 'the Act'). The Assessing Officer, vide order dated 25.01.1996, raised a demand for a sum of Rs. 14,73,91,000/- with regard to the sum payable to the PSUs while holding that the Respondent has not acted as a broker in the transactions carried out for the Indian Bank rather as an independent dealer and that there was no overriding title in favour of the PSU's with regard to the additional amount earned out of the securities transactions and it is a case of application of income after accrual and, hence, the said amount is liable to be assessed as the income of the Respondent. B C D

(e) The Respondent, being dissatisfied with the order, preferred an Appeal before the Commissioner for Income Tax (Appeals). Learned Commissioner of Income Tax (Appeals), vide order dated 08.08.1996, set aside the demand for additional tax while deciding the issue in favour of the Respondent and held that the alleged additional interest payable to the PSUs could not be considered as the income of the Respondent. E

(f) Being aggrieved by the order dated 08.08.1996, the Revenue filed an appeal bearing No. ITA No.2297(Mds)/1996 before the Income Tax Appellate Tribunal (hereinafter referred to as 'the Tribunal'). The Tribunal, vide order dated 05.01.2005, allowed the appeal filed by the Revenue and held that the amount received at the hands of the Respondent which is alleged to be payable to the PSUs is the income of the Respondent and there is no overriding title exists in favour of the PSUs so as to cause diversion of income. F G

(g) It is pertinent to note that in the meanwhile criminal proceedings which were initiated with respect to the present transactions in question against the Respondent along with others bearing No. CC 17 of 1997, was decided on 27.04.2004 by the CBI court. The court, while acquitting H

- A the Respondent has observed that the relationship between the Indian Bank and the Respondent is that of principal-agent and with regard to the transactions in question the Respondent acted in the capacity of a broker and not as an individual dealer. However, the Tribunal refused to rely on the evidence produced in the trial court on the ground that the assessment proceedings are different from the criminal proceedings and
- B the evidence adduced in the trial court couldn't be relied to absolve the Respondent from the tax liability.

- (h) Being aggrieved by the order of the ITAT dated 05.01.2005, the assessee filed Tax Case Appeal No. 368 of 2005 before the High Court. The High Court, vide order dated 29.10.2012, set aside the order
- C of the Tribunal while relying on the evidence given in the criminal case in this regard. Hence, this appeal is filed before this Court.

Point(s) for consideration:-

4. The only point for consideration before this Court is whether
- D on the facts and circumstances of the present case the High Court was right in holding that the alleged additional interest payable to PSUs cannot be assessed as income of the Respondent?

Rival contentions:-

5. Learned counsel appearing on behalf of the Revenue contended
- E that the High Court erred in relying on the evidence given in the criminal proceedings as the nature of the criminal proceedings is different from that of assessment proceedings. Learned counsel further contended that the High Court, while passing impugned judgment, relied on the letter dated 25.03.1994 of M/s Indian Bank. However, the High Court
- F failed to consider the factual position that out of 8 PSUs only 3 have confirmed the receipt of demand drafts. The remaining 5 PSUs denied to have received any such Demand Draft either from Shri T. Jayachandran, the Respondent or from M/s Indian Bank and the High Court was not justified in accepting the Respondent's contention that there was some overriding title in favour of the PSUs in the alleged
- G additional interest payable to them by the Indian Bank.

6. Learned counsel for the Revenue finally contended that the impugned judgment is bad in law on the facts and circumstances of the present case and requires to be set aside by this Court.

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7. *Per contra*, learned senior counsel appearing for the Respondent submitted that the role of the Respondent was only that of a conduit for taking demand drafts in respect of additional interests payable to the PSUs and the demand draft taken on behalf of the Indian Bank did not form part of the total income of the Respondent and there exists an overriding title in favour of the PSUs with reference to the amount in question i.e., the additional interest payable to the PSUs. A
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8. Learned senior counsel further submitted that though the assessment proceedings are different in nature from that of criminal proceedings but the same could not be a ground to throw out the legitimate conclusion arrived at by the trial court on the basis of proved evidence. Learned senior counsel finally submitted that the High Court was right in taking note of the developments in the criminal case in coming to the conclusion that the respondent was acting as a broker or agent to the Indian Bank and the order of the High Court was well within the parameters of law and requires no interference. C

9. We have heard learned counsel for both the parties and perused the factual matrix of the case. D

Discussion:-

10. The answer to the short question whether the alleged interest payable to the PSUs can be assessed as an income of the Respondent depends on the determination of true nature of relationship between the Indian Bank and the Respondent with regard to the transactions in question and the capacity in which he held the amount of 14,73,91,000/-. Now, coming to the question of relationship between the Indian Bank and the Respondent, the normal settlement process in Government securities is that during transaction banks make payments and deliver the securities directly to each other. The broker's only function is to bring the buyer and seller together and help them to negotiate the terms for which he earns a commission from both the parties. He does not handle either cash or securities. In this respect, the broker functions like the broker in the inter bank foreign exchange market. The conduct of the Respondent in the transaction in question cannot be termed to be strictly within the normal course of business and the irregularities can be noticed from the manner in which the whole transactions were conducted. However, the same cannot be basis for holding the Respondent E
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A liable for tax with regard to the sum in question and what is required to be seen is whether there accrued any real income to the Respondent or not.

11. It is required to be seen in what capacity the Respondent held the said amount-independently or on behalf of the Indian Bank. The Assessing Officer, while passing order dated 25.01.1996, has held that there exists no agreement between the Respondent and the Indian Bank about the payment of additional interest to the PSUs and there was no overriding title in respect of the additional interest for the PSUs. However, the position in this regard is very much settled that an agreement need not be in writing but can be oral also and the same can be inferred from the conduct of the parties.

12. Further, while considering the claim of the Respondent and the view of the Assessing Officer, how the bank itself had treated the Respondent, is a matter of relevance. At the outset, learned counsel appearing on behalf of the Revenue contended that the proceedings under the Income Tax Act are independent proceedings and the High Court committed a grave error in relying on the findings of the criminal Court. We do not find any force in the contention of the appellant herein as the High Court has not held that the findings of the criminal court are binding on the Revenue authorities. Rather the High Court was of the view that the findings arrived at by the criminal court can be taken into consideration while deciding the question as to the relationship between the parties to the case. When the findings are arrived by a criminal court on the evidence and the material placed on record then in absence of anything shown to the contrary, there seems to be no reason as to why these duly proved evidence should not be relied upon by the Court. The High Court has specifically appraised the findings given by the CBI Court in this regard. The relationship between the Indian Bank and the Respondent is very much clear by the evidence led during the criminal proceedings. The Executive Director of the Bank has specifically spoken about the role of the Respondent as a broker specifically engaged by the Bank for the purchase of securities and that the Bank has included the interest money too in the consideration paid, for the purpose of taking demand drafts in favour of PSUs. Further, the evidence led by other bank officials points out that the price of securities itself were fixed by the bank authorities and as per their directions the Respondent had purchased the securities at the market price and the differential amount

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was directed to be used for taking demand drafts from the bank itself for paying additional interest to the PSUs. Further, the letter dated 25.03.1994 by the Bank wherein the Bank had acknowledged the receipt of Demand Drafts taken by the Respondent gives an unblurred picture about the capacity of the Respondent in holding the amount in question. Consequently, the conduct of the parties, as is recorded in the criminal proceedings showing the receipt of amount by the broker, the purpose of receipt and the demand drafts taken by the broker at the instance of the bank are sufficient to prove the fact that the Respondent acted as a broker to the Bank and, hence, the additional interest payable to the PSUs could not be held to be his property or income. A
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13. The income that has actually accrued to the Respondent is taxable. What income has really occurred to be decided, not by reference to physical receipt of income, but by the receipt of income in reality. Given the fact that the Respondent had acted only as a broker and could not claim any ownership on the sum of Rs. 14,73,91,000/- and that the receipt of money was only for the purpose of taking demand drafts for the payment of the differential interest payable by Indian Bank and that the Respondent had actually handed over the said money to the Bank itself, we have no hesitation in holding that the Respondent held the said amount in trust to be paid to the public sector units on behalf of the Indian Bank based on prior understanding reached with the bank at the time of sale of securities and, hence, the said sum of Rs. 14,73,91,000/- cannot be termed as the income of the Respondent. In view of the above discussion, the decision rendered by the High Court requires no interference. C
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14. In view of the above discussion, the appeal is hereby dismissed with no orders as to cost. In view of the above, all the connected appeals are also disposed of accordingly. F