

M/S. MUTHOOT LEASING AND FINANCE LIMITED
AND ANOTHER

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v.

COMMISSIONER OF INCOME TAX

(Civil Appeal Nos. 10201-10202 of 2010)

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JANUARY 03, 2023

[SANJIV KHANNA AND M. M. SUNDRESH, JJ.]

Interest Tax Act, 1974 – s.2(5-A) and s.2(5-B) – Hire-purchase agreements – Appellants-assesseees are credit institutions within meaning of s.2(5-A) – Whether appellants-assesseees liable to pay tax on interest component included in hire-purchase instalments paid under hire-purchase agreements – ITAT referred to CBDT Circular No. 760 dated 13th January 1998 and observed that hire-purchase agreement is a composite transaction, and has elements of bailment and sale and appellants-assesseees are not liable to pay interest tax as hire instalments are not interest on loans and advances that is chargeable to interest tax – High Court reversed the finding of ITAT, observing that hire-purchase instalment includes “finance charges”, which is nothing but interest, and therefore, interest tax is leviable on the interest component – The transaction, though styled as a hire-purchase agreement, the High Court held, is in fact a finance agreement for purchase of a vehicle – Reliance placed by appellant-assessee on Circular No. 760 dated 13th January 1998 issued by CBDT was rejected by the High Court – On appeal, held: Given the dictum and ratio in the cases of Sahara India Savings and Investment Corporation Limited and State Bank of Patiala Through General Manager, the view taken by High Court is not correct – In Circular No. 760 dated 13th January 1998, the CBDT observed that they considered the issue and were advised that in case of transactions which are, in substance, in the nature of hire-purchase, the receipts of hire charges would not be in the nature of interest – In transactions which are, in substance, in the nature of financing transactions, the hire charges should be treated as interest, subject to interest tax – To determine the distinction between the two transactions, the assessing officers were required to consider the issue on merits taking, inter alia, into account – (i) the terms of the agreement; (ii) the nature of the arrangement between the supplier

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- A of the asset, the hire-purchase company and the end user of the asset; and (iii) the intention of the parties which manifests itself in the fixation of the initial payment, the method of determination of hire-purchase price etc – However, when hire-purchase company pays the price or a substantial part thereof on behalf of such hirer who is real purchaser but does not pay the full price, then such
- B agreement is in nature of a security for re-payment of the loan and is essentially a loan transaction – High Court reversed finding of ITAT without framing a specific substantial question of law and thus, interference with findings of fact was unwarranted – Orders passed by ITAT deleting the additions made by assessing officer in
- C case of appellant, set aside – Motor Vehicles Act 1988 – s.51.

Interest Tax Act, 1974 – s.2(7) – Interpretation & scope of – Interest recovered under hire-purchase agreement, if falls under s.2(7) – Held: s.2(7) has been interpreted in two decisions, that is, in the cases of Sahara India Savings and Investment Corporation

- D *Limited and State Bank of Patiala Through General Manager, which have given a very limited and restricted meaning to s.2(7) of the Act as interest directly arising “on” loans and advances, and not any other interest, be it interest earned on investment or interest payable on delayed payment of the discounted bill of exchange.*

- E *Hire-Purchase – Elements – Held: A hire-purchase agreement has two elements – an element of bailment and an element of sale – Any transfer or sale made by the hirer or any violation of the hire-purchase agreement can lead to civil as well as criminal consequences.*

- F *Taxation – Taxation matters – Interference by High Court with findings of fact recorded by the ITAT – Scope – Held: Findings of fact generally recorded by the ITAT are treated as conclusive – The High Court can interfere with the findings of fact while deciding a substantial question of law when the findings are not supported by the material on record, so as to be treated as perverse – For this,*
- G *the High Court must frame a separate substantial question of law and only then interfere with the findings of fact by the ITAT, while applying the strict parameters.*

- H *Taxation matters – Precedents – Rule of caution when applying the ratio of judgments relating to one tax enactment as a precedent*

in a case relating to another tax enactment – This rule of caution is important and should not be overlooked, more so when the language of the enactment and the object and purpose of the enactment are different.

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Constitution of India – Art.141 – SLP – Dismissal of – Held: If the dismissal is in limine and at the admission stage, it would not constitute a binding precedent u/Art.141 of the Constitution.

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Allowing the appeals, the Court

HELD : 1. A hire-purchase agreement has two elements – an element of bailment and an element of sale. The element of sale fructifies when the option to purchase is exercised by the intending purchaser after fulfilling the terms of the agreement. Till then, the goods are given on hire. One can argue that in a hire-purchase, an element of interest is inbuilt, but what is payable is the hire amount and not interest *per se*. The hirer has an option to return the vehicle or the goods taken on hire. It is not a simple transaction of giving a loan or advance on which interest is payable. The transaction(s) in commercial and legal sense are far more complex with corresponding rights of the parties. Even if the hirer is recorded as the owner of the vehicle under Section 51 of the MV Act, the name of the appellant – assessee is also recorded in the registration book, which is in recognition of the hire-purchase agreement. The registered owner under the MV Act may be liable in case of accidents/traffic challans, etc. But this, in no way, dilutes the right of the appellants – assessees in respect of the title of the property, that is, the vehicle. Any transfer or sale made by the hirer or any violation of the hire-purchase agreement can lead to civil as well as criminal consequences. Given the dictum and ratio in *Sahara India Savings and Investment Corporation Limited* and *State Bank of Patiala Through General Manager*, the view taken by the High Court of Delhi in *M/s GE. Capital Transportation*, as followed by the High Court of Delhi in *Commissioner of Interest Tax v. M/S GE. Capital Transportation* is correct and the view taken by the High Court of Kerala in the impugned judgment is not in consonance with the above decisions of this court. [Para 14][329-C-H]

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A 2. In Circular No. 760 dated 13th January 1998, the CBDT
observed that they considered the issue and were advised that
in case of transactions which are, in substance, in the nature of
hire-purchase, the receipts of hire charges would not be in the
nature of interest. In transactions which are, in substance, in the
B nature of financing transactions, the hire charges should be
treated as interest, subject to interest tax. To determine the
distinction between the two transactions, the assessing officers
were required to consider the issue on merits taking, inter alia,
into account – (i) the terms of the agreement; (ii) the nature of
the arrangement between the supplier of the asset, the hire-
C purchase company and the end user of the asset; and (iii) the
intention of the parties which manifests itself in the fixation of
the initial payment, the method of determination of hire-purchase
price etc. However, when the hire-purchase company pays the
price or a substantial part thereof on behalf of such hirer who is
D the real purchaser but does not pay the full price, then such
agreement is in the nature of a security for re-payment of the
loan and is essentially a loan transaction. [Para 16][331-F-H;
332-A-B]

3.1. The judgment in *Sundaram Finance Limited* relates to
the true nature of hire in hire-purchase agreements as in the
E context of the sales tax enactment. In the present case, however,
one is dealing with and interpreting Section 2(7) of the Act, which
has been interpreted in two decisions, that is, in the case of *Sahara
India Savings and Investment Corporation Limited* and *State Bank
of Patiala Through General Manager*, which have given a very
F limited and restricted meaning to Section 2(7) of the Act as
interest directly arising “on” loans and advances, and not any
other interest, be it interest earned on investment or interest
payable on delayed payment of the discounted bill of exchange.
[Para 17][332-B-E]

G 3.2. Taxation depends upon the language of the charging
section and what is brought to tax within the four corners of the
charging section. Therefore, one should be careful and cautious
when applying the ratio of judgments relating to one tax enactment
as a precedent in a case relating to another tax enactment. This
H rule of caution is important and should not be overlooked, more

so when the language of the enactment and the object and purpose of the enactment are different. [Para 18][332-E-F] A

4.1. Findings of fact generally recorded by the ITAT are treated as conclusive. The High Court can interfere with the findings of fact while deciding a substantial question of law when the findings are not supported by the material on record, so as to be treated as perverse. For this, the High Court must frame a separate substantial question of law and only then interfere with the findings of fact by the ITAT, while applying the strict parameters. In the present case, the High Court did not frame a specific substantial question of law and thus, the interference with the findings of fact is unwarranted. This is not to say that the tax authorities are not entitled to examine the surrounding facts and circumstances to ascertain the true character and nature of the transaction, regardless of the nomenclature given by the parties. [Para 19][333-C-E] B C

4.2. In the present case, at this distinct point of time, it would not be appropriate to pass an order of remand. It is to be also noted that the Act has ceased to operate with effect from 31st March 2000. 21. The impugned judgment is accordingly set aside. The additions made by the assessing officer are set aside and the orders passed by the ITAT deleting the additions in the case of appellant and other cases are upheld. [Paras 20, 21] [333-G; 334-A] D E

Commissioner of Income Tax, Kanpur v. Sahara India Savings and Investment Corporation Limited (2009) 17 SCC 43 and State Bank of Patiala Through General Manager v. Commissioner of Income Tax, Patiala (2015) 15 SCC 483 : [2015] 12 SCR 243 – relied on. F

The Commissioner of Income Tax, Cochin v. M/s. Muthoot Leasing & Finance Limited [Judgment dated 10th March, 2008 of High Court of Kerala in ITA No. 269 of 2002] – overruled. G

State Bank of Mysore v. Commissioner of I.T., Karnataka-I, Bangalore (1989) 175 ITR 607 – held overruled. H

A *Commissioner of Income Tax v. Cholamandalam Investment and Finance Co. Ltd.* (2008) 296 ITR 601 – held approved.

B *K.L. Johar and Co. (In Both Appeals) v. Deputy Commercial Tax Officer, Coimbatore III (In Both Appeals)* AIR 1965 SC 1082 : [1965] 2 SCR 112;
Sundaram Finance Limited v. State of Kerala and Another AIR 1966 SC 1178 : [1966] 2 SCR 828;
Commissioner of Interest Tax, New Delhi v. M/s G.E. Capital Services India [Decision of Supreme Court dated 16th May, 2008 in SLP(C) No. 14202 of 2008] and *Association of Leasing and Financial Service Companies v. Union of India and Others* (2011) 2 SCC 352 : [2010] 13 SCR 381 – referred to.

Case Law Reference

D	[1966] 2 SCR 828	referred to	Para 7
	(2009) 17 SCC 43	relied on	Para 10
	[2015] 12 SCR 243	relied on	Para 10
E	[1965] 2 SCR 112	referred to	Para 15
	[2010] 13 SCR 381	referred to	Para 18

CIVIL APPELLATE JURISDICTION : Civil Appeal Nos.10201-10202 of 2010.

F From the Judgment and Order dated 10/03/2008 of the High Court of Kerala at Ernakulam in ITA Nos.230 and 269/2002.

With

G Civil Appeal Nos.10203, 10204, 10205-10206, 10207 of 2010, 4903, 4904, 4905, 4906, 4907 Of 2014 And Slp (Civil) No.4441 of 2011.

Rupesh Kumar, Shashank Bajpai, Chinmayee Chandra, A. Raghunath, Ms. Ritika Sinha, V. K. Monga, E. M. S. Anam, A. N. Arora, Mrs. Anil Katiyar, Advs. for the appearing parties.

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The Judgment of the Court was delivered by A

SANJIV KHANNA, J.

1. Leave granted in Special Leave Petition (Civil) No. 4441 of 2011.

2. The common question which arises for consideration in this batch of Civil Appeals is: whether the appellants – assesseees are liable to pay tax under the Interest-Tax Act, 1974¹ on the interest component included in the hire-purchase instalments paid under the hire- purchase agreement? B

3. The facts, in brief, are that the appellants – assesseees are non-banking finance and leasing companies registered with the Reserve Bank of India. Some of the appellants – assesseees have been reclassified as hire-purchase finance companies. It is not disputed that the appellants – assesseees are credit institutions within the meaning of Section 2(5-A) of the Act, which reads as follows: C D

“(5-A) “credit institution” means,—

(i) a banking company to which the Banking Regulation Act, 1949 (10 of 1949), applies (including any bank or banking institution referred to in Section 51 of that Act); E

(ii) a public financial institution as defined in Section 4- A of the Companies Act, 1956 (1 of 1956);

(iii) a State financial corporation established under Section 3 or Section 3-A or an institution notified under Section 46 of the State Financial Corporations Act, 1951 (63 of 1951), and F

(iv) any other financial company;”

It is also imperative to mention Section 2(5-B) of the Act, which defines a “financial company” and includes within its ambit hire-purchase finance companies: G

“(5-B) “financial company” means a company, other than a company referred to in sub-clause (i), (ii) or (iii) of clause (5-A), being—

¹For short, ‘the Act’.

- A (i) a hire-purchase finance company, that is to say, a company which carries on, as its principal business, hire-purchase transactions or the financing of such transactions;

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- B 4. The contention of the appellants – assesseees is that under a hire- purchase agreement, they hire out a vehicle to the customer and receive hire-purchase instalments, and not interest on loans and advances. As per the findings of fact recorded by the Income Tax Appellate Tribunal², the hirer has acknowledged that the appellants– assesseees are the owners of the vehicle. As per the hire-purchase agreements, the
- C hirer must pay rent to the owner during the hiring as per the sums mentioned in the agreement on the dates mentioned therein. Further, the hirer has to take proper care of the vehicle and keep it in good condition. He has to also pay all rents, rates, taxes and outgoings payable. The
- D hirer must keep the vehicle in his sole custody and possession at the address mentioned in the agreement, or such other place as the owner has previously consented to in writing. The owner or any person authorised by him in writing is entitled to inspect the vehicle at all reasonable times during the period of hire. The hirer may, at any time, determine the hire-purchase agreement by delivering the vehicle at his
- E own cost to the owners. If the hirer fails to pay the hire instalments within the stipulated time, becomes insolvent, pledges or sells, or attempts to pledge or sell or otherwise alienate or transfer the vehicle, or does or suffer any act or thing whereby, or in consequence of which, the vehicle may be distrained, seized or taken into execution under legal process, or breaks or fails to perform or observe any condition as mentioned in the
- F hire-purchase agreement, the owner is entitled to forthwith determine the agreement and, thereupon, entitled to enter the place where the vehicle is kept and seize, remove and retake possession thereof. The owner is also entitled to sue for all the instalments due, damages for breach of the agreement, and the cost in retaking possession of the
- G vehicle. The owners, if agreeable, may permit the hirer to have the registration of the vehicle in his own name, provided that the hirer shall transfer the registration in the name of the owner whenever required to do so by the owner, especially when the hirer commits breach of any of

² For short, ‘ITAT’.

the conditions of the agreement, due to which the owners are obliged to seize the vehicle. A

5. On these facts, the ITAT accepted the plea of the appellants – assesseees that they are not liable to pay interest tax on the interest component imbedded in the hire-purchase instalment. The ITAT referred to Circular No. 760 dated 13th January 1998 issued by the Central Board of Direct Taxes³ and observed that the hire-purchase agreement is a composite transaction, and has elements of bailment and sale. Relying on the terms and conditions of the hire- purchase agreement noted above, the ITAT held that hire-purchase agreements are distinguishable from loans and advances. The hire instalments are something different and more, and not the interest on loans and advances that is chargeable to interest tax. B C

6. The ITAT had also relied on the provisions of The Hire-Purchase Act, 1972, which, in our opinion, is palpably wrong as the said enactment was never enforced and was subsequently repealed *vide* the Hire-Purchase (Repeal) Act, 2005. D

7. The High Court of Kerala in the case of *The Commissioner of Income Tax, Cochin v. M/s. Muthoot Leasing & Finance Limited*⁴ by the impugned judgment dated 10th March 2008 set aside and reversed the finding of the ITAT, observing that the hire- purchase instalment includes “finance charges”, which is nothing but interest, and therefore, interest tax is leviable on the interest component. The transaction, though styled as a hire-purchase agreement, the High Court held, is in fact a finance agreement for purchase of a vehicle. The hirer, as a borrower, had been charged a flat rate of interest. The hirer, on payment of instalments, had the option to purchase the vehicle for one rupee, which was an empty formality, because the vehicle was already registered in his name. As per Section 51 of the Motor Vehicles Act, 1988⁵, the registering authority is required to enter the details of the hire-purchase agreement in the certificate of registration. The respondent – assessee therein had the license to repossess the vehicle on default, but to get ownership they had to apply for change in name under the provisions of E F G

³ For short, ‘CBDT’.

⁴ ITA No. 269 of 2002.

⁵ For short, the ‘MV Act’.

- A the MV Act. Reliance placed by the appellant – assessee on Circular No. 760 dated 13th January 1998 issued by the CBDT was rejected, observing that the CBDT had earlier issued Circular No. 738 dated 25th March 1996 clarifying that the interest recovered under the hire-purchase agreement falls under Section 2(7) of the Act. For arriving at the conclusion, reliance was placed on the decision of this Court in ***Sundaram Finance Limited v. State of Kerala and Another***⁶, a decision which we will subsequently examine.

- C 8. The High Court of Delhi in ***Commissioner of Interest Tax v. M/s G.E. Capital Transportation***⁷, decided on 1st September 2006, has taken a different view, observing that the assessee therein having not earned any interest on loan or advance, no component of the hire-purchase instalment paid by the customer/hirer towards the hire is chargeable to interest tax under the Act. At this stage, it may be relevant to state that the special leave petition preferred by the Commissioner of Income Tax, New Delhi against the decision of the Delhi High Court in a connected matter, in the case of ***Commissioner of Income Tax, New Delhi v. M/s G.E. Capital Services India***⁸, was dismissed by this Court on 16th May 2008. The dismissal being *in limine* and at the admission stage, would not constitute a binding precedent under Article 141 of the Constitution of India.

- E 9. Section 2(7) of the Act, post amendment with effect from 1st October 1991, reads as under:

“(7) “interest” means interest on loans and advances made in India and includes—

- F (a) commitment charges on unutilised portion of any credit sanctioned for being availed of in India; and
- (b) discount on promissory notes and bills of exchange drawn or made in India,
- G but does not include—
- (i) interest referred to in sub-section (1-B) of Section 42 of the Reserve Bank of India Act, 1934 (2 of 1934);

⁶ AIR 1966 SC 1178.

⁷ ITA No. 1275 of 2006.

H ⁸ SLP(C) No. 14202 of 2008.

(ii) discount on treasury bills;” A

10. There are two direct decisions of this Court interpreting Section 2(7) of the Act *vide Commissioner of Income Tax, Kanpur v. Sahara India Savings and Investment Corporation Limited*⁹; and *State Bank of Patiala Through General Manager v. Commissioner of Income Tax, Patiala*¹⁰, which are relevant, and thus, we would refer to them in some detail. B

11. In *Sahara India Savings and Investment Corporation Limited* (supra), this Court noticed that prior to 1st October 1991, the word “interest” in Section 2(7) was defined so as to include any amount chargeable to income tax under the head “Interest on Securities”. Post the amendment, the words “amount chargeable to income tax... under the head ‘Interest on Securities’” stood deleted. The Act, this Court held, had been enacted with twofold purposes, namely, as an anti-inflationary measure and for revenue collection. With this objective in mind, the court proceeded to examine and interpret Section 2(7) of the Act to hold that the expression “interest” must be given a restrictive meaning as interest on “loans and advances, including commitment charges, discount on promissory notes and bills of exchange, but not to include interest referred to in Section 42(1-B) of the Reserve Bank of India Act, 1934 as well as discount on treasury bills”. Section 2(7) defines taxable interest in the first part and confines the interest only to loans and advances, and in the second part includes, by specific mandate, commitment charges and discounts on promissory notes and bills of exchange. Interpreting the provision in this manner, it was held that the legislature, in its wisdom, had extended the meaning of the word “interest” in the second part to two items, namely, commitment charges and discounts on promissory notes and bills of exchange. In the said case, the respondent – assessee had made investments in bonds and debentures. It was held that interest on these bonds and debentures bought by the respondent – assessee therein, as and by way of “investment”, is not taxable as interest under Section 2(7) of the Act as they do not qualify and could not be treated as “interest on loans and advances”. C D E F G

12. In *State Bank of Patiala Through General Manager* (supra), this Court had examined the cleavage of opinion between different High

⁹ (2009) 17 SCC 43.

¹⁰ (2015) 15 SCC 483.

- A Courts on whether the fixed percentage charge leviable on default in payment of discounted bills of exchange should be treated as interest within the meaning of Section 2(7) of the Act. The amount credited on this account had been booked by the appellant Bank therein in its interest account. Agreeing with the assessee therein, this Court observed that
- B the definition of ‘interest’ in the Act is a narrow one, and is exhaustive as it is a “means and includes” definition. The reasoning of the Karnataka High Court in *State Bank of Mysore v. Commissioner of I.T., Karnataka-I, Bangalore*¹¹ that discounting of a bill is a form of advance or loan and hence, compensation paid on delayed payment of money due thereon is interest on loans and advances, was overruled as
- C overlooking the limited coverage in Section 2(7) of the Act. There is a distinction between loans and advances, and discounted bills of exchange drawn or made in India. If discounted bills of exchange were also to be treated as loans and advances made in India, there would be no need to extend the definition of “interest” to include discount on bills of exchange.
- D This Court, accordingly, agreed with the views expressed by some other High Courts, including Madras High Court in *Commissioner of Income Tax v. Cholanandalam Investment and Finance Co. Ltd.*¹², that the character of an overdue bill is not synonymous with the loans and advances and, therefore, it will not fall within the ambit and scope of interest under part one of Section 2(7) of the Act. It was observed that
- E the right to charge for overdue interest by the assessee Banks therein did not arise on account of any delay in repayment of any loan or advance, but arose on account of default in the payment of amounts due under a discounted bill of exchange. A subject can be brought to tax only by a clear statutory provision in that behalf. Interest is chargeable to tax under
- F the Act only if it arises “directly” from a loan or advance and not otherwise. Accordingly, interest payable “on” a discounted bill of exchange cannot be equated with interest payable “on” a loan or advance.

- G 13. The decision in *State Bank of Patiala Through General Manager* (supra) also draws distinction between the broad definition of the expression “interest” in the Income Tax Act, 1961 *vide* Section 2(28-A), to observe that the expression used under the Act, that is the Interest-Tax Act, 1974, is much narrower and restricted. Under the Income Tax

¹¹ (1989) 175 ITR 607.

¹² (2008) 296 ITR 601.

Act, 1961, interest can be payable in any manner whatsoever. Secondly, the expression “in respect of” includes interest arising even indirectly out of a money transaction, unlike the word “on” contained in Section 2(7) of the Act, which connotes a direct arising of payment of interest out of a loan or advance. Thirdly, “any moneys borrowed” must be contrasted with “loan or advances”. The former expression would include moneys borrowed by means other than by way of loans or advances. Thus, the Act, unlike the Income Tax Act, 1961, is focused on a very narrow taxable event which does not include within its ken interest payable on default in payment of amounts due under a discounted bill of exchange.

14. A hire-purchase agreement has two elements – an element of bailment and an element of sale. The element of sale fructifies when the option to purchase is exercised by the intending purchaser after fulfilling the terms of the agreement. Till then, the goods are given on hire. One can argue that in a hire-purchase, an element of interest is inbuilt, but what is payable is the hire amount and not interest *per se*. The hirer has an option to return the vehicle or the goods taken on hire. It is not a simple transaction of giving a loan or advance on which interest is payable. The transaction(s) in commercial and legal sense are far more complex with corresponding rights of the parties. Even if the hirer is recorded as the owner of the vehicle under Section 51 of the MV Act, the name of the appellant – assessee is also recorded in the registration book, which is in recognition of the hire-purchase agreement. The registered owner under the MV Act may be liable in case of accidents/traffic challans, etc. But this, in no way, dilutes the right of the appellants – assessees in respect of the title of the property, that is, the vehicle. Any transfer or sale made by the hirer or any violation of the hire-purchase agreement can lead to civil as well as criminal consequences. Given the dictum and ratio in *Sahara India Savings and Investment Corporation Limited* (supra) and *State Bank of Patiala Through General Manager* (supra), the view taken by the High Court of Delhi in *M/s G.E. Capital Transportation*¹³ (supra), as followed by the High Court of Delhi in *Commissioner of Interest Tax v. M/S G.E. Capital Transportation*¹⁴, is correct and the view taken by the High court of Kerala in the impugned judgment is not in consonance with the above decisions of this court.

¹³ ITA 1275 of 2006.

¹⁴ ITA 1280 of 2006.

A 15. However, the learned counsel for the Revenue has relied on
Sundaram Finance Limited (supra), which decision had also been
relied upon by the High Court of Kerala in the impugned judgment. The
submission is that there is a conflict in the ratios. Before we consider the
ratio of the judgment in *Sundaram Finance Limited* (supra), we would
B refer to the decision of the Constitution Bench of this Court in *K.L.*
Johar and Co. (In Both Appeals) v. Deputy Commercial Tax Officer,
*Coimbatore III (In Both Appeals)*¹⁵. In the decision, this Court had
referred to the concept of hire-purchase in the context of sales tax liability
under the Madras General Sales Tax Act, 1939, to observe that the hirer
C can exercise the option of purchase only when he fulfils the terms of the
agreement, and till then there is no sale at all. The argument, which was
accepted by the High Court of Madras, that because in most cases such
option is exercised by the hirer, the tax was leviable immediately, was
D flawed, as the taxable event had not taken place. In the said case also,
one of the contentions raised was that only one rupee had to be paid as
the price for the transfer of the vehicle since the entire amount was paid
as hire. This contention was not accepted, for it overlooked the essence
of the hire-purchase agreement, which was that the hire includes not
only what would be payable really as hire but also that a part of it was
E towards the price. These observations are relevant in the context of the
present case as they refer to and explain the true nature of hire in hire-
purchase agreements, *albeit* in the context of the sales tax enactment.
However, this court also observed that even in the absence of legislative
guidance, the sales tax authorities may split the hire into two parts. This
decision was followed in the case of *Sundaram Finance Limited* (supra)
with the majority judgment authored by J.C. Shah, J. observing that the
F decision of the Constitution Bench in *K.L. Johar and Co.* (supra) dealt
with the agreements where the financier has paid the balance amount to
the erstwhile owner of the goods and thereupon obtained the hire-
purchase agreement from the customer, under which the customer
becomes the owner of the goods on payment of all the instalments of the
G stipulated hire and exercising his option to purchase the goods on payment
of a nominal price. In another form of hire-purchase transactions, goods
are purchased by the customer who, in consideration of executing a
hire-purchase agreement and allied documents, remains in possession
of the goods, subject to the liability to pay the amount paid by the financier

H ¹⁵ AIR 1965 SC 1082.

on behalf of the customer to the owner or the dealer. The financier obtains the hire-purchase agreement which gives him a license to seize the goods in the event of failure by the customer to abide by the conditions of the hire-purchase agreement. The true effect of a transaction may be determined from the terms of the agreement considered in light of the surrounding circumstances. In some cases, the real bargain would be a loan on the security of the goods. If there is a *bona fide* and completed sale of goods, evidenced by documents, anterior to and independent of a subsequent and distinct hiring to the vendor, the transaction may not be regarded as a loan transaction, even though the reason why it was entered into was to raise money. Recording the aforesaid, the appeal of the assessee in ***Sundaram Finance Limited*** (supra) was allowed by the majority observing that they were carrying on business of financiers and not dealing with motor vehicles. The motor vehicle purchased by the customer was registered in his name and remained, at all material times, so registered in his name. The sale letter was a formal document which was not made effective by registering the vehicle in the name of the assessee and even the insurance of the motor vehicle had to be effected as if the customer was the owner.

16. Before we examine the reasoning and context in which the elucidation was made, we would like to refer to two circulars issued by the CBDT. The CBDT had, *vide* Circular No. 738 dated 25th March 1996, opined that hire-purchase transactions are generally in the nature of finance transactions entered into by the companies engaged in the business of financing, and finance charges accruing or arising to hire-purchase finance companies are in the nature of interest as defined in Section 2(7) of the Act and hence, chargeable to interest tax. However, in the subsequent Circular No. 760 dated 13th January 1998, the CBDT observed that they considered the issue and were advised that in case of transactions which are, in substance, in the nature of hire-purchase, the receipts of hire charges would not be in the nature of interest. In transactions which are, in substance, in the nature of financing transactions, the hire charges should be treated as interest, subject to interest tax. To determine the distinction between the two transactions, the assessing officers were required to consider the issue on merits taking, *inter alia*, into account – (i) the terms of the agreement; (ii) the nature of the arrangement between the supplier of the asset, the hire-purchase company and the end user of the asset; and (iii) the intention

- A of the parties which manifests itself in the fixation of the initial payment, the method of determination of hire-purchase price etc. However, when the hire-purchase company pays the price or a substantial part thereof on behalf of such hirer who is the real purchaser but does not pay the full price, then such agreement is in the nature of a security for re-payment of the loan and is essentially a loan transaction. Reference was made to the judgment in the case of **Sundaram Finance Limited** (supra).
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17. As noticed above, this judgment in **Sundaram Finance Limited** (supra) relates to the true nature of hire in hire-purchase agreements as in the context of the sales tax enactment. In the present case, however, we are dealing with and interpreting Section 2(7) of the Act, which has been interpreted in two decisions, that is, in the case of **Sahara India Savings and Investment Corporation Limited** (supra) and **State Bank of Patiala Through General Manager** (supra), which have given a very limited and restricted meaning to Section 2(7) of the Act as interest directly arising “on” loans and advances, and not any other interest, be it interest earned on investment or interest payable on delayed payment of the discounted bill of exchange.
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18. Taxation depends upon the language of the charging section and what is brought to tax within the four corners of the charging section. Therefore, one should be careful and cautious when applying the ratio of judgments relating to one tax enactment as a precedent in a case relating to another tax enactment. This rule of caution is important and should not be overlooked, more so when the language of the enactment and the object and purpose of the enactment are different. This ratio is somewhat expressed by this Court in **Association of Leasing and Financial Service Companies v. Union of India and Others**¹⁶, wherein in the context of levy of service tax by Section 65(105)(zm) read with section 65(12) of the Finance Act, 1994, as amended, banking and financial services were brought to tax. In the context of the said enactment, this Court deemed it appropriate to distinguish between financial lease and operating lease and held that the services rendered in the former case would be taxable, whereas the latter would fall out of the tax net. In this context, it was observed that non-banking financial companies are essentially loan companies, but they could, in addition
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H ¹⁶ (2011) 2 SCC 352.

thereto, be in the business of equipment leasing, hire- purchase finance and investment. In case of bailment termed as “hire”, the bailee receives both possession of the chattel and the right to use it in return for remuneration. On the other hand, equipment leasing is long-term financing which helps the borrower to raise funds without outright payment in the first instance. Here, the “interest” element cannot be compared to consideration for lease/hire, which is in the nature of remuneration (consideration) for hire.

19. Findings of fact generally recorded by the ITAT are treated as conclusive. The High Court can interfere with the findings of fact while deciding a substantial question of law when the findings are not supported by the material on record, so as to be treated as perverse.¹⁷ For this, however, the High Court must frame a separate substantial question of law and only then interfere with the findings of fact by the ITAT, while applying the strict parameters. In the present case, the High Court did not frame a specific substantial question of law and thus, the interference with the findings of fact is unwarranted. This is not to say that the tax authorities are not entitled to examine the surrounding facts and circumstances to ascertain the true character and nature of the transaction, regardless of the nomenclature given by the parties.

20. Given the aforesaid legal position, we may have even remanded the matter to the assessing officer for fresh adjudication and to re-examine all the transactions in light of the aforesaid ratio and reasoning, keeping in mind the dictum laid in **Sahara India Savings and Investment Corporation Limited** (supra) and **State Bank of Patiala Through General Manager** (supra) to rule out cases where camouflage or subterfuge has been adopted to avoid payment of interest tax. This would have entailed not only looking at the documents but also several other factors, which would have meant getting information and ascertainment of facts in detail from the assessee and the hirer. However, at this distinct point of time, we do not think that it would be appropriate to pass an order of remand. It is to be also noted that the Act has ceased to operate with effect from 31st March 2000.

¹⁷ See *Karnataka Board of Wakf v. Anjuman-E-Ismail Madris-Un-Niswan*, (1999) 6 SCC 343; and *C. Doddanarayana Reddy (Dead) By Legal Representatives and Others v. C. Jayarama Reddy (Dead) By Legal Representatives and Others*, (2020) 4 SCC 659.

A 21. Recording the aforesaid, we allow the present appeals and set aside the impugned judgments. The additions made by the assessing officer are set aside and the orders passed by the ITAT deleting the additions in the case of the appellant – M/s. Muthoot Leasing and Finance Limited and other cases are upheld. In the facts of the present case, there would be no order as to costs.

Bibhuti Bhushan Bose
(Assisted by : Neha Sharma, LCRA)

Appeals allowed.