Rajasthan State Warehousing ... vs Commissioner Of Income-Tax on 23 February, 2000

Author: Syed Shah Mohammed Quadri

Bench: S.S.M.Quadri, D.P.Wadhwa

PETITIONER:
RAJASTHAN STATE WAREHOUSING CORPORATION

Vs.

RESPONDENT:
COMMISSIONER OF INCOME-TAX

DATE OF JUDGMENT: 23/02/2000

BENCH:
S.S.M.Quadri, D.P.Wadhwa

JUDGMENT:

SYED SHAH MOHAMMED QUADRI, J.

This appeal arises from the judgment and order of the Division Bench of the High Court of Judicature for Rajasthan Bench at Jaipur in Income-tax Reference No.86 of 1987 dated November 9, 1993. The assessee is the appellant. By the order under challenge the High Court answered the following question, referred to it under Section 256(1) of the Income Tax Act, 1961 (for short the Act), in the affirmative, that is, in favour of the Revenue and against the assessee:

> Whether on the facts and in the circumstances of the case and the business of the assessee being one and indivisible, the Tribunal was right in law in holding that the expenses have to allocated in the same percentage as the different sources of income and are not to be allowed in entirety as allowed by the Commissioner of Income-tax (A) after following decisions noted in para 11 of the order dated 31.01.1985 for the assessment years 1974-75, 1975-76 and 1980-81?

In the assessment year 1977-78 the appellant, a State Government Corporation, derived its income from interest, letting out the warehouses and administrative charges for procurement of foodgrains while working for the Food Corporation of India as well as the State Government. It claimed deduction of expenditure of Rs.38,13,555.17 under Section 37 of the Act in computing its income under the head profits and gains of business of business or profession. The Income Tax Officer allowed only so much of the expenditure as could be allocated to the taxable income and disallowed

the rest of it which was referable to the non-taxable income, being exempt under Section 10(29) of the Act. On appeal, the Commissioner of Income Tax (Appeals)-II accepted the claim of the appellant that the entire expenditure was deductible. The Revenues appeal therefrom to the Income-tax Appellate Tribunal was allowed upholding the order of the Income Tax Officer on July 17, 1986. At the instance of the appellant the question noted above was referred to the High Court. By order under challenge the High Court confirmed the order of the Income-tax Appellate Tribunal. Hence this appeal. Mr. Joseph Vellapally, learned senior counsel appearing for the appellant, relied on the judgments of this Court in Commissioner of Income-tax, Madras Vs. Indian Bank Ltd. [56 ITR 77], Commissioner of Income-tax, Bombay City I Vs. Maharashtra Sugar Mills Ltd. [82 ITR 452] and of Punjab and Haryana High Court in Punjab State Co-operative Supply and Marketing Federation Ltd. Vs. Commissioner of Income-tax, Patiala-I [128 ITR 189] in support of his contention that the order of the High Court is unsustainable. The contention of Mr.K.N. Shukla, learned senior counsel appearing for the Revenue, is that the expenditure which is attributable to the exempted income is not a permissible deduction and it has been rightly disallowed by the High Court. To appreciate the contentions of the learned counsel it may be useful to refer to Section 37(1) of the Act: 37. General. - (1) Any expenditure (not being expenditure of the nature described in Sections 30 to 36 * * * and not being in the nature of capital expenditure or personal expenses of the assessee), laid out or expended wholly and exclusively for the purposes of the business or profession shall be allowed in computing the income chargeable under the head Profits and gains of business or profession.

A plain reading of the above provision makes it clear that it is a residuary provision and allows an expenditure, not covered under Sections 30 to 36, in computing the income chargeable under the head profits and gains of business or profession, provided its other requirements are satisfied. They are : (i) the expenditure should not be in the nature of capital expenditure or personal expenses of the assessee;

(ii) it should have been laid out or expended wholly and exclusively for the purposes of the business or profession; and (iii) it should have been expended in the previous year. The disallowance of the expenditure was not for non-compliance of requirements of Section 37(1) of the Act but for the reason that the expenditure was incurred on an activity from which income was exempted under the Act. A similar question arose in the case of Indian Bank Limited (supra). In that case the respondent-assessee, in the course of its business, borrowed moneys for investment in securities. Part of its income, derived from securities, was exempt under the Income Tax Act, 1922 (for short the Act of 1922). It sought to deduct the interest paid on the entire borrowed amount. The question before this Court was whether a portion of the interest, which was referable to investment on securities from which income was exempt, was allowable. Section 10(2)(iii) and (xv) of the Act of 1922, was precursor of Section 37(1) of the Act. It was held by this Court that in allowing a deduction which was permissible one need not look beyond the expenditure to see whether it had the quality of directly or indirectly producing taxable income and, therefore, there was no warrant for disallowing a proportionate part of the interest referable to money borrowed for the purchase of securities yielding tax free interest. That judgment was followed in the case of Maharashtra Sugar Mills Ltd. (supra). There the assessee-company was manufacturing sugar in its factory and was also growing sugar-cane for purposes of its factory. On the question of deduction of expenditure, so much of the

managing agency commission which was referable to the growing of sugar-cane, was disallowed on the ground that the income from sugar-cane cultivation was agricultural income and not exigible to tax. The Appellate Tribunal found that the cultivation of sugar-cane and the manufacture of sugar by the assessee constituted one single and indivisible business. It was held by this Court that the entire managing agency commission was laid out for the purpose of the business carried on by the assessee and was allowable under Section 10(2)(xv) of the Act of 1922 and that the fact that the income from growing of sugar-cane, a part of that business was not taxable under the Act, was not a relevant circumstance. The third case cited by Mr. Vellapally is of Punjab and Haryana High Court in Punjab State Co-operative Supply and Marketing Federation Ltd. case (supra). The judgment in that case shows that on the question of apportionment of the expenditure, with reference to the activity which yielded income and with reference to the activity which did not yield income, the High Court, taking note of the finding recorded by the Tribunal that the business of the assessee was one and indivisible and following the aforesaid decisions of this Court, held that the entire expenditure incurred by the assessee was deductible. Mr. Shukla, however, placed reliance on the judgment of the Division Bench of the Madras High Court in Waterfall Estates Ltd. Vs. Commissioner of Income-tax, Madras (No.1) [131 ITR 207] which was affirmed by this Court in Waterfall Estates Ltd. Vs. Commissioner of Income-tax [219 ITR 563]. That was a case under Section 37(1) of the Act. The assessee in that case was carrying on different ventures, profits from some of them were taxable and from the other were exempt under the Act. In respect of the earlier assessment years expenditure with reference to each activity was worked out separately without claiming any expenditure referable to the head-office. In the assessment year 1965-66 the assessee claimed deduction of the entire expenditure including that relating to the head-office. The finding recorded by the Tribunal was that there was no proof that different ventures constituted the same business. On that finding the Tribunal took the view that the apportionment of the expenditure was valid. The High Court of Madras confirmed the order of the Tribunal and the same was upheld by this Court. There, it is evident, the result turned against the assessee due to absence of the finding of fact that different ventures carried on by it constituted one indivisible business, which meant that there was no nexus between the venture in question and the business comprising of other ventures carried from the head office and therefore so much of the expenditure incurred on the head office which was attributable to that venture was not a permissible deduction in computing profits of the business. Indeed, such expenditure does not properly fall within the meaning of the expenditure laid out or expended wholly and exclusively for the purpose of the business or professional. In view of the above discussion, the following principles may be laid down : (i) if income of an assessee is derived from various heads of income, he is entitled to claim deduction permissible under the respective head whether or not computation under each head results in taxable income; (ii) if income of an assessee arises under any of the heads of income but from different items e.g. different house properties or different securities etc., and income from one or more items alone is taxable whereas income from the other item is exempt under the Act, the entire permissible expenditure in earning the income from that head is deductible; and (iii) in computing profits and gains of business or profession when an assessee is carrying on business in various ventures and some among them yield taxable income and the others do not, the question of allowability of the expenditure under Section 37 of the Act will depend on : (a) fulfilment of requirements of that provision noted above; and (b) on the fact whether all the ventures carried on by him constituted one indivisible business or not; if they do the entire expenditure will be a permissible deduction but if they do not the principle of apportionment of the expenditure will apply

because there will be no nexus between the expenditure attributable to the venture not forming integral part of the business and the expenditure sought to be deducted as the business expenditure of the assessee. Mr. Shukla has fairly conceded that if the exempted income and the taxable income are earned from one and indivisible business then the apportionment of the expenditure cannot be sustained. But, submits the learned counsel, in this case the Tribunal did not record a finding that the business of the assessee is one indivisible, therefore, the apportionment of the expenditure is valid. We are afraid, we cannot accede to the contention of the learned counsel inasmuch as a plain reading of the question itself shows that it embodies -- the business of the assessee being one and indivisible. This being the position, it is not open to the Revenue to contend that the business is not one and indivisible. In view of the fact that a perusal of the question itself discloses that income from various ventures is earned in the course of one and indivisible business, the impugned order upholding the apportionment of the expenditure and allowing deduction of only that proportion of it which is referable to taxable income, is unsustainable. We, therefore, answer the question in the negative, that is, in favour of the assessee and against the Revenue. The order under appeal is accordingly set aside and the appeal is allowed with costs.