

## IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

## TAX APPEAL No. 556 of 2013

## FOR APPROVAL AND SIGNATURE:

*HONOURABLE Mr. JUSTICE AKIL KURESHI**and**HONOURABLE Ms. JUSTICE SONIA GOKANI*

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- 1 Whether Reporters of Local Papers may be allowed to see the judgment ?
  - 2 To be referred to the Reporter or not ?
  - 3 Whether their Lordships wish to see the fair copy of the judgment ?
  - 4 Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 or any order made thereunder ?
  - 5 Whether it is to be circulated to the civil judge ?
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ANUPAM TELE SERVICES....Appellant(s)

*Versus*

INCOME TAX OFFICER....Opponent(s)

*Appearance:*

Mr. MANISH J SHAH, Advocate for the Appellant(s) No. 1

Mr. SUDHIR M MEHTA, Advocate for the Opponent(s) No. 1

**CORAM:** HONOURABLE Mr. JUSTICE AKIL KURESHI

and

HONOURABLE Ms. JUSTICE SONIA GOKANI22<sup>nd</sup> January 2014**ORAL JUDGMENT** (PER : HONOURABLE Mr. JUSTICE AKIL KURESHI)

Appeal is admitted for consideration of following substantial question

of law :-

**“Whether on the facts and in the circumstances of the case, the Tribunal was right in law in holding that Section 40A(3) applies to the payment of Rs. 33,10,194/= deposited by the Appellant in the bank account of Tata Tele Services Limited ?”**

We have heard learned counsel for final disposal of the appeal. Brief facts are as under :-

The issue pertains to A.Y 2006-07. The appellant-assessee is involved in the business of distribution of mobile and recharge vouchers of Tata Teleservices Limited. They are the authorized channel partners of the Company. They would make payment to the company for purchase of recharge vouchers. The assessee made such payment through account payee cheques till 22<sup>nd</sup> August 2005, when a circular was issued by Tata Teleservices Limited requiring the appellant to deposit cash at the company's office at Surat.

During scrutiny assessment, the Assessing Officer noticed that the assessee had made a total payment of Rs. 33,10,194/= during the year under consideration to Tata Teleservices Limited by cash on different dates and such payment exceeded Rs. 20,000/= each. He also noticed that similar payments exceeding Rs. 20,000/= in cash were made to one Rajvi Enterprises totalling Rs. 1,37,368/= and one payment to Messrs. R.D Infotech of Rs. 31,350/=.

*Prima facie* believing that such cash payments exceeding Rs. 20,000/= would be hit by section 40A(3) of the Income-tax Act, 1961 {"Act" for short}, the Assessing Officer issued a notice to the assessee why such expenses should not be disallowed.

In response to such notice, the assessee contended that it was purchasing re-charge vouchers from Tata Teleservices Limited. The said company issued a Circular dated 22<sup>nd</sup> August 2005 and instructed the assessee to deposit cash at its office at Surat. Yet another letter was written on 1<sup>st</sup> September 2005 instructing the assessee to deposit cash and not make payments by cheque or demand draft. The reason why Tata Teleservices Limited were not accepting payment by Banker's cheque or Demand Draft was that the assessee had an account with a Cooperative Bank. It was assured that the cash payment would be deposited in the Bank on behalf of the assessee. It was pointed out that not only the present assessee but all the channel partners/distributors of Tata Teleservices Limited in Gujarat were required to make such cash payments. It was pointed out that if the assessee continued to make payment through Cheque or Demand Draft, they would get the recharge vouchers only after 4-5 days which would effect their business. It was contended that the intention of Section 40A(3) is to prevent deduction on bogus payments. The assessee had made cash deposits with a reputed public limited

company, which they were liable to do as per the terms and condition of agreement with the company which they had followed.

The Assessing Officer, however, was not convinced by such reply and held that the payments in cash exceeding Rs. 20,000/= violate the provision of Section 40A(3) of the Act and disallowed 20% of Rs. 34,78,912/= and thus, added back a sum of Rs. 6,95,782/= to the total income of the assessee.

The assessee carried the matter in appeal. CIT [A], by his order dated 12<sup>th</sup> November 2009, reversed the decision of the Assessing Officer. He held and observed as under :-

“6. I have gone through the submission of the appellant and the observations of the Assessing Officer. The fact of cash payment is not disputed. It is a fact that Tata Tele Services Limited had intimated that the DD/Payee Order issued by the assessee’s banker namely Saraswat Cooperative Bank Limited would be accepted as a cheque and effect delivery after the cheques are cleared which will take 4/5 days. This delay might adversely affect the business of the assessee. The a is a Distributor of Tata Tele Services Limited and can obtain the recharge facilities only after payment made to the principal company. Therefore, the Tata Tele Services Limited insisted the company to pay in cash and get immediate delivery to avoid delay and suffering in the market. From 28.08.2005, in accordance with the instruction of Tata Tele Services Limited, the amounts were paid in cash. Such circumstances need to be kept in mind. The factum of payment made to the Tata Tele Services Limited is not disputed. The transactions are genuine. The assessee had filed a copy of account of Tata Tele Services Limited which clearly

supports that the payments were made. It has been held by the various courts that where genuineness of transactions and identity of receivers is established the payments should not be disallowed. It is not the case of the Assessing Officer that the transactions are not genuine nor the payments were not made. Considering the circumstances, the assessee took a very practical step in making the payment to stay in business in a competitive environment. It is not a case where by making such payments the objective underlined in section 40A(3) has been frustrated. The objective of section 40A(3) requiring such payments to be made by crossed cheques or drafts has been repeatedly stressed by the Courts as per example in *Walford Transport [Eastern India] v. CIT (1999) 240 ITR 902 (Gua)* as under :-

“From a perusal of the decision of different High Courts referred to above, it clearly emerges that the purpose of section 40A(3) of the Act is not to penalized the assessee for making cash payment of an amount of Rs. 2,500/= or above. The purpose is only preventive and to check evasion of tax and flow of unaccounted money or to check transactions which are not genuine and may be put as camouflage to evade tax by showing fictitious or false transactions.”

6.1 The conduct of the assessee in making payments to Tata Teleservices Limited being genuine is not inconsistent with the above stated objectives. Therefore, the disallowance under section 40A(3) in respect of payment made to Tata Teleservices Limited is deleted.

6.2 As regards payments made to Rajvi Enterprise and R.D Infocom are concerned, the same has been genuinely made to the above parties and in some cases are covered by circumstances notified in Rule 6DD particularly Rude DD (j) of the I.T Rules, 1962. Therefore, the disallowance under section 40A(3) is not warranted in respect of such genuine payments. Now, the Assessing Officer officer is directed to delete the addition on this account.”

Revenue carried the matter in appeal before the Tribunal. Tribunal allowed the Revenue's appeal. In particular, the Tribunal took into account clause (j) of Rule 6DD of the Income Tax Rules, 1962, which at the relevant time after amendment, read as under :-

“6DD. No disallowance under sub-section (3) of section 40A shall be made where any payment in a sum exceeding two thousand five hundred rupees is made otherwise than by crossed cheque drawn on a bank or by a crossed bank draft in the cases and circumstances specified hereunder, namely :-

(j) where the payment was required to be made on a day on which the banks were closed either on account of holiday or strike.”

The Tribunal concluded as under :-

*“The Hon'ble jurisdictional High Court in the case of Hasanand Pinjomal [Supra] had interpreted the old provisions of Rule 6DD only. The decision of the Special Bench, Calcutta in the case of Kenaram Saha & Subhas Saha [Supra] is the latest decision on the applicability of the provisions of Section 40A (3) and is squarely applicable to the facts of this case according to which the assessee can get exemption from the provision of Section 40A(3) only if he is able to show that his case falls within any of the clauses of Rule 6DD of the Income Tax Rules. It has further been held in that case that burden to establish under which particular clause his case falls is also on the assessee. Since the lower authorities have not examined the issue in hand in the light of this decision, we are of the considered opinion that*

*the matter should go back to the file of the A.O for fresh adjudication to decide the issue in the light of the decisions of Kenaram Saha & Subhas Saha [Supra]. This ground of the revenue is allowed for statistical purpose.*

16. *In the combined result, assessee's appeal is allowed and Revenue's appeal is allowed for statistical purpose."*

The assessee is therefore in appeal before us.

Learned advocate Shri J.P Shah appearing for the appellant has submitted that any payment made in cash to Tata Teleservices Limited was on account of the directives issued by the said Company. The assessee had a bank account in a cooperative bank which resulted in delayed release of the amount in favour of the principal. This in turn would delay the assessee getting the recharge vouchers. M/s. Tata Teleservices Limited had indicated that such payments would be deposited on behalf of the assessee in the bank account. He, therefore, submitted that there was no breach of section 40A (3) of the Act. The whole intention behind enactment of the said provision is to curb black money transactions. In the present case when there was no doubt about the genuineness of the payments made and that such payments are reflected in the accounts of the payer as well as payee, rigors of Section 40A (3) should not have been applied. Counsel relied on the decision of the Apex Court in case of *Attar Singh Gurmukh Singh v. Income-Tax Officer, Ludhiana*, reported in [1991] 191

ITR 667 in which it was observed that, "*the terms of section 40A (3) are not absolute. Consideration of business expediency and other relevant factors are not excluded. Genuine and bona fide transactions are not taken out of the sweep of the section.*"

Counsel also relied on the decision of Punjab & Haryana High Court reported in 350 ITR 227 in which under somewhat similar circumstances, the Court upheld the view of the Tribunal in not applying Section 40A(3) of the Act to the cash payments when ultimately, such amounts were deposited in the bank by the payee.

On the other hand, Shri Sudhir Mehta, learned counsel for the respondent opposed the appeal contending that the payments made by the assessee were clearly covered under section 40A(3) of the Act. The resultant effect therefore must be allowed to be operated. He would rely on Rule 6DD of the Income-tax Rules, 1962 to contend that none of the clauses contained in the said rule would apply in the present case.

He relied on the following decisions :-

[a] *Attar Singh Gurmukh Singh v. Income-Tax Officer, Ludhiana*, reported in [1991] 191 ITR 667, in which it was observed that the word "*expenditure*" has not been defined in the Act. It is a word of wide import. Section 40A(3) refers to the expenditure incurred by the assessee in respect of which payment is made.



It means that all outgoings are brought under the word “*expenditure*” for the purpose of the section. It was observed that any restraint intended to curb the chances and opportunities to use or create black money should not be regarded as curtailing the freedom of trade or business.

[b] In case of Commissioner of *Income-Tax v. Hynoup Food & Oil Industries Private Limited*, reported in [2007] 290 ITR 702 (Guj), wherein, the Division Bench of this Court, in a reference from the Income Tax Tribunal on a question of law, had an occasion to interpret Section 40A(3) read with Rule 6DD in which, it was observed as under :-

“16. Whether in the circumstances of the present case is it possible to state that the case of the assessee is governed by the exceptions carved out by Rule 6DD(j) of the Rules ? The Rule has to be read in the context of the second proviso to sub-section (3) of Section 40A of the Act whereunder a disallowance is not permissible if on consideration of business expediency an assessee is able to satisfy the Assessing Officer that he was required to make payment in cash due to exceptional or unavoidable circumstances, or because payment by a crossed cheque or bank draft was not practicable, and/or would have caused genuine difficulty to the payee, having regard to the nature of the transaction and the necessity for expeditious settlement thereof, and further furnishes evidence to the satisfaction of the Assessing Officer as to the genuineness of the payment and the identity of the payee. Thus, the position is that even if business expediency is established by the assessee concerned, the assessee would be required to show that payment by a crossed cheque or bank draft was not possible due to exceptional or unavoidable circumstances and also furnish evidence to establish genuineness of the transaction and identity of the payee; in the second situation also, after showing business expediency the assessee would be required to establish that it was necessary to make payment in cash because either the payment

by crossed cheque or bank draft was not practicable, or would have caused genuine difficulty to the payee, and such impracticability or difficulty to the payee is with regard to the nature of the transaction and the necessity for immediate settlement of the transaction, and simultaneously satisfying the Assessing Officer as to the genuineness of the payment and the identity of the payee.

17. In other words, genuineness of the payment and the identity of the payee are the first and foremost requirement. Even if business expediency gets established, in absence of evidence as to genuineness of the payment and identity of the payee, an assessee cannot seek recourse to either of the two situations laid down in clause (j) of Rule 6DD of the Rules."

In case of *Nathalal Jethalal v. Commissioner of Income-Tax*, reported in [1993] 199 ITR 757, Division Bench of this Court, relying on the decision in case of *Attar Singh Gurmukh Singh* [Supra] held that section 40A(3) would be attracted to payments made for acquiring stock-in-trade and other materials.

In case of *K. Abdu & Company v. Income-tax Officer, Ward-3, Cannanore*, reported in [2008] 170 Taxman 297 (Ker), wherein, Kerala High Court held that where the assessee made cash payments to the bank accounts of suppliers maintained with different banks, such payments would not be excluded from section 40A(3) of the Act.

In case of *Commissioner of Income-tax, Madurai v. Venkatadhri Constructions*, reported in [2013] 31 Taxmann.com 71 [Madras] in which similar view was expressed.

We need to answer the question on the facts arising in the present case

with the help of the decisions listed before us. The facts before us are more or less undisputed.

The appellant-assessee acted as an agent of Tata Teleservices Limited for distributing mobile cards and recharge vouchers. For getting such mobile cards and recharge vouchers, the assessee would make payment to Tata Teleservices Limited. Till a point of time, in the month of August 2005, such payments were made by account payee cheques. The Tata Teleservices Limited, however, issued a circular not only to the assessee but to all other distributors in the State stating that the distributors will pay only through demand draft drawn on nationalized bank or through bank deposit slips and where the distributor had a bank account with cooperative bank, the payment should be made in cash., In consonance with such Circular, Tata Teleservices Limited wrote a letter to the assessee and stated as under :-

*“We further intimate you that your bank is “The Saraswat Cooperative Bank Limited. We treat D.D/Pay order from your bank as a cheque and your invoice processes done after credit balance in Company’s account. It will take 4/5 days. It will suffer our business. So please deposit cash at Public Office of Company in Surat and get immediate delivery to avoid suffering of market. We will deposit your cash in our bank on behalf of you. You are very well known that we cannot suffer our business at any cost.”*

In terms of such circular and letter, the assessee thereafter made cash

payments to Tata Teleservices Limited. About the genuineness of payments made, there is no dispute. The full account of the assessee as well as Tata Teleservices Limited were placed on record. The assertion of the assessee that such monies were to be deposited by Tata Teleservices Limited in their bank account and were eventually so deposited were not disputed. It is precisely on this premise that the appellate Commissioner observed that the *factum* of payment to Tata Teleservices Limited is not disputed and the transactions were genuine. The assessee had in fact filed a copy of the accounts with Tata Teleservices Limited indicating that such payments were made.

Section 40A (3) of the Act pertains to expenses or payments not deductible in certain circumstances. The said section, as prevalent at the relevant time, read thus :-

“(3)(a) Where the assessee incurs any expenditure in respect of which payment is made in sum exceeding twenty thousand rupees otherwise than by an account payee cheque drawn on a bank or account payee bank draft, no deduction shall be allowed in respect of such expenditure;

(b) Where an allowance has been made in the assessment for any year in respect of any liability incurred by the assessee for any expenditure and subsequently during any previous year (hereinafter referred to as subsequent year) the assessee makes payment in respect thereof, otherwise than by an account payee cheque drawn on a bank or account payee bank draft, the

payment so made shall be deemed to be the profits and gains of business or profession and accordingly chargeable to income-tax as income of the subsequent year if the amount of payment exceeds twenty thousand rupees :

Provided that no disallowance shall be made and no payment shall be deemed to be the profits and gains of business or profession under this sub-section where any payment in a sum exceeding twenty thousand rupees is made otherwise than by an account payee cheque drawn on a bank or account payee bank draft, in such cases and under such circumstances as may be prescribed, having regard to the nature and extent of banking facilities available, considerations of business expediency and other relevant factors."

Rule 6DD of the Income Tax Rules, 1962 provides for situations under which disallowance under section 40A (3) shall not be made and no payment shall be deemed to be the profits and gains of business or profession under the said section. Amongst the various clauses, clause (j) which is relevant, read as under :-

*(j) where the payment was required to be made on a day on which the banks were closed either on account of holiday or strike;*

It could be appreciated that Section 40A and in particular sub-clause (3) thereof aims at curbing the possibility of on-money transactions by insisting

that all payments where expenditure in excess of a certain sum [*in the present case twenty thousand rupees*] must be made by way of account payee cheque drawn on a bank or account payee bank draft.

As held by the Apex Court in case of *Attar Singh Gurmukh Singh* [Supra], “..In our opinion, there is little merit in this contention. Section 40A(3) must not be read in isolation or to the exclusion of rule 6DD. The section must be read along with the rule. If read together, it will be clear that the provisions are not intended to restrict the business activities. There is no restriction on the assessee in his trading activities. Section 40A(3) only empowers the Assessing Officer to disallow the deduction claimed as expenditure in respect of which payment is not made by crossed cheque or crossed bank draft. The payment by crossed cheque or crossed bank draft is insisted on to enable the assessing authority to ascertain whether the payment was genuine or whether it was out of the income from undisclosed sources. The terms of section 40A(3) are are not absolute. Considerations of business expediency and other relevant factors are not excluded. Genuine and bona fide transactions are not taken out of the sweep of the section. It is open to the assessee to furnish to the satisfaction of the Assessing Officer the circumstances under which the payment in the manner prescribed in section 40A (3) was not practicable or would have caused genuine difficulty to the payee. It is also open to the assessee to identify the person who has received the cash payment. Rule 6DD provides that an assessee can be exempted from

*the requirement of payment by a crossed cheque or crossed bank draft in the circumstances specified under the rule. It will be clear from the provisions of section 40A(3) and rule 6DD that they are intended to regulate business transactions and to prevent the use of unaccounted money or reduce the chances to use black money for business transactions."*

It was because of these considerations that this Court in case of *Hynoup Foods Private Limited* [Supra] observed that the genuineness of the payment and the identify of the payee are the first and foremost requirements to invoke the exceptions carved out in rule 6DD(j) of the Income-tax Rules, 1962.

In the present case, neither the genuineness of the payment nor the identity of the payee were in any case doubted. These were the conclusions on facts drawn by the Appellate Commissioner. The Tribunal also did not disturb such facts but relied solely on Rule 6DD (j) of the Rules to hold that since the case of the assessee did not fall under the said exclusion clause nor was covered under any of the clauses of Rule 6DD, consequences envisaged in Section 40A(3) of the Act must follow.

In our opinion, the Tribunal committed an error in coming to such a conclusion. We would base our conclusions on the following reasons :-

[a] The paramount consideration of Section 40A(3) is to curb and reduce the possibilities of black money transactions. As held by the Supreme Court in

*Attar Singh Gurmukh Singh* [Supra], section 40A(3) of the Act does not eliminate considerations of business expediencies.

[b] In the present case, the appellant assessee was compelled to make cash payments on account of peculiar situation. Such situation was as follow -

[i] the principal company, to which the assessee was a distributor, insisted that cheque payment from a cooperative bank would not do, since the realization takes a longer time;

[ii] the assessee was, therefore, required to make cash payments only;

[iii] Tata Teleservices Limited assured the assessee that such amount shall be deposited in their bank account on behalf of the assessee;

[iv] It is not disputed that the Tata Teleservices Limited did not act on such promise;

[v] if the assessee had not made cash payment and relied on cheque payments alone, it would have received the recharge vouchers delayed by 4/5 days and thereby severely affecting its business operations.

We would find that the payments between the assessee and the Tata Teleservices Limited were genuine. The Tata Teleservices Limited had insisted



that such payments be made in cash, which Tata Teleservices Limited in turn assured and deposited the amount in a bank account. In the facts of the present case, rigors of section 40A(3) of the Act must be lifted.

We notice that the Division Bench of the Rajasthan High Court in case of *Smt. Harshila Chordia vs. Income-Tax Officer*, reported in [2008] 298 ITR 349 (Raj) had observed that the exceptions contained in Rule 6DD are not exhaustive and that the said rule must be interpreted liberally.

Before closing, we may clarify that the above observations would apply only to the cash payments made by the assessee to the Tata Teleservices Limited. No such peculiar facts arise in case of payments made to the other two agencies *viz.*, Rajvi Enterprise and R.D Infocom. Learned counsel for the appellant also clarified that this appeal is confined to only the payments made to Tata Teleservices Limited and no others.

In the result, the question is answered in favour of the appellant assessee and against the Revenue. Judgment of the Tribunal is reversed. Tax Appeal is allowed. Order accordingly.

{Akil Kureshi, J.}

{Ms. Sonia Gokani, J.}

Prakash\*