

PETITIONER:
ATTAR SINGH GURMUKH SINGH

Vs.

RESPONDENT:
INCOME TAX OFFICER, LUDHIANA ETC.

DATE OF JUDGMENT 07/08/1991

BENCH:
SHETTY, K.J. (J)
BENCH:
SHETTY, K.J. (J)
YOGESHWAR DAYAL (J)

CITATION:
1991 AIR 2109 1991 SCR (3) 405
1991 SCC (4) 385 JT 1991 (3) 352
1991 SCALE (2) 254

ACT:
Income Tax Act, 1961/Income Tax Rules, 1962--Section 40A(3)/ Rule 6DD--Validity of--Applicability to payments made for acquiring stock-in-trade.

HEADNOTE:

The assesses in these appeals have made payments in cash exceeding a sum of Rs.2500 for some of the purchases of stock-in-trade. So while computing the income of the assesses under the head "profits and gains of business" the assessing authority disallowed deduction on account of such payments held to be in contravention of the terms of section 40A(3) of the Income Tax Act, 1961 read with the Rule 6DD of the Income Tax Rules, 1962.

The assesseees have challenged the same. So in the instant case the question under consideration before this Court is (i) the validity of section 40A(3) of the Act (ii) the applicability of section 40A(3) to payments made for acquiring stock-in-trade.

Originally section 40A(3) required payments in respect of expenditure which exceeded Rs.2500 to be made by a crossed cheque or crossed bank draft and by the Amending Act 1987 to remove hardships to smaller assesseees the said amount has been raised to Rs. 10,000, Section 40A(3) begins with a non-obstante clause so the legislature has made it clear that the provisions of section 40A(3) are overriding and operate inspite of any thing to the contrary contained in any other provisions of the Act relating to the computation of income under the head "profits and gains of business or profession". Sub-section (3) empowers the assessing authority to disallow as deduction of any expenditure in respect of which payment is made in cash exceeding Rs. 10,000 otherwise than by a crossed cheque or crossed bank draft.

Rule 6DD of Income Tax Rules, 1962 provides for cases and circumstances in which payment of a sum exceeding Rs. 10,000 may be made otherwise than by crossed cheque or by a crossed demand draft.

The assesseees challenged on the ground that provisions of section

40A(3) intend to restrict the business activities. Dismissing the appeals and Special Leave Petition, the Court,

HELD: That section 40A(3) must not be read in isolation or to the exclusion of Rule 6DD. This section must be read along with the Rule 6DD and if read together it is clear that the provisions of the section are not intended to restrict the business activities. It only empowers the assessing officer to disallow the deductions claimed as expenditure in respect of which payment is not made by crossed cheque or crossed bank draft. The same is insisted only to enable the assessing authority to ascertain whether it was out of the income from disclosed sources and even the terms of section 40A(3) are not absolute. Considerations of business expediency and other relevant factors are not excluded, since it is open to the assessee to furnish the circumstances under which the payment was not practicable or would have caused genuine difficulty to the payee. 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. Thus section 40A(3) and Rule 6DD are intended to regulate the business transactions and to prevent the use of unaccounted money or reduce the chance to use black money for business transactions. Moreover while interpreting a taxing statute the Court cannot be oblivious of the proliferation of black money which is in circulation in our country- Thus any restraint intended to use or create black should not be regarded as curtailing the freedom of trade or business. [409G-410E]

The term expenditure as per section 40A(3), means all outgoing including the expenditure incurred for purchasing the stock-in-trade. Since to determine the gross profits the value of the stock-in-trade has to be taken into account. So payments can be disallowed if they are made in cash in the sums exceeding the amount specified under section 40A(3) and also not provided for exemption under Rule 6DD. Thus section 40A(3) is attracted to payments made for acquiring stock-in-trade and other materials. [410G-411A]

Sajwanlal Jaiswal v. CIT, [1976] 103 ITR 706 Orissa; U.P. Hardware Store v. CIT, [1976] 104 ITR 664; Allahabad; Ratan Udyog v. ITO, [1977] 109 I.T.R. 1 Allahabad; P.R. Textiles v. CIT Kerala, [1980] 121 ITR 237 Kerala; CIT v. Kishan Chand Maheswari Dass, [1980] 121 ITR 232 P & H; Kanti Lal purshottam & Co. v. CIT, [1985] 155 ITR 519 Raj; CIT v. New Light Tin Mfg. Co., [1980] 121 ITR 229 P & H; Fakri Automobiles v. CIT, [1986] 160 ITR 504 Raj; 407

Venkata Satayanarayana Timber Depot v. ITR, [1987] 165 ITR 253 AP. and Akash Films v. CIT, [1991] ITR 32 Karnataka, approved.

CIT v. Hardware Exchange, [1991] 190 ITR 61, reversed.

JUDGMENT:

CIVIL APPELLATE JURISDICTION: Civil Appeal No. 11 of 1991.

From the Judgment and Order dated 15.10.1979 of the Punjab and Haryana High Court in C.Q.P. No. 1009 of 1974.

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Civil Appeal Nos. 2752/79, 1105/76, 29 & 985/87, 4950/89, 1032/79, 3331/83, SLP (Civil) No. 15/80, CMP. No. 1350/80 and C.A. No. 1425 of 1976.

B. Sen, G.C. Sharma, S.K. Mehta, C.S. Aggarwal, BV. Desai, Ms. Radha Rangaswamy, K.C. Dua, Umesh Khaitan, Darshan Singh. Praveen Kumar, M.M. Kashyap and S.K. Bagga for the Appellants.

J. Ramamurthy, B.B. Ahuja and Ms. A. Subhashini for the Respondents.

The Judgment of the Court was delivered by

K. JAGANNATHA SHETTY, J. The assessee in these appeals have made payments in cash exceeding a sum of Rs.2500 for some of the purchases of stock-in-trade. The payments are not allowed as deductions in the computation of income under the head "profits and gains of business". The payments are held to be in contravention of the terms of Section 40A(3) of the Income Tax Act, 1961 read with the Rule 6DD of the Income Tax Rules, 1962. The assessee has appealed to this Court challenging the disallowance.

Two questions arise for consideration in these appeals; (i) The validity of Section 40A(3) of the Act; and (ii) The applicability of Section 40A(3) to payments made for acquiring stock-in-trade.

Section 40A(3) so far as material provides:

"40A. Expenses or payments not deductible in certain circumstances--(1) The provisions of this section shall have effect notwithstanding anything to the contrary contained in any other provision of this Act relating to the computation of income under the head "Profits and Gains of business or profession."

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(3) Where the assessee incurs any expenditure in respect of which payment is made, after such date (not being later than the 31st day of March 1969) as may be specified in this behalf by the Central Government by notification in the Official Gazette, in a sum exceeding ten thousand rupees otherwise than by a crossed cheque drawn on a bank or by a crossed bank draft, such expenditure shall not be allowed as a deduction:

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Provided further that no disallowance under this subsection shall be made where any payment in a sum exceeding ten thousand rupees is made otherwise than by a crossed cheque drawn on a bank or by a crossed 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."

Originally, Section 40A(3) required payments in respect of expenditure, which exceed Rs.2,500 to be made by a crossed cheque or a crossed bank draft. On failure to do so, the payments made were disallowed in the computation of income. In order to remove hardship to smaller assessee, the Amending Act, 1987, has raised this ceiling to Rs. 10,000. Section 40A(3) begins with a non-obstante clause. It is an overriding provision which operates in spite of anything to the contrary contained in any other provision of the Act relating to the computation of income under the head "profits and gains of business or profession". The legislature has thus made it clear that the provisions of Section 40A will apply in supersession of other contrary provisions of the Act relating to the computation of income. Sub-sec-

tion (3) empowers the assessing officer to disallow, as a deduction any expenditure in respect of which payment is made of any sum exceeding Rs. 10,000 otherwise than by a crossed cheque or crossed bank draft.

Rule 6DD of the Income Tax Rules, 1962 refers to cases and circumstances in which payment of a sum exceeding Rs. 10,000 may be made otherwise than by a crossed cheque or by a crossed bank draft. The Rule so far as it is relevant reads:

"6DD. Cases and circumstances in which payment in a sum exceeding ten thousand rupees may be made otherwise

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than by a crossed cheque drawn on a bank or by a crossed bank draft--No disallowance under sub-section (3) of Section 40 A shall be made where any payment in a sum exceeding ten thousand 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:

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(j) in any other case, where the assessee satisfies the Assessing Officer that the payment could not be made by a crossed cheque drawn on a bank or by a crossed bank draft--

(1) due to exceptional or unavoidable circumstances; or

(2) because payment in the manner aforesaid was not practicable, 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 also furnishes evidence to the satisfaction of the Assessing Officer as to the genuineness of the payment and the identity of the payee."

As to the validity of Section 40A(3) it was urged that if the price of the purchased material is not allowed to be adjusted as against the sale price of the material sold for want of proof of payment by a crossed cheque or crossed bank draft, then the income tax levied will not be on the income but it will be on an assumed income. It is said that the provision authorising levy tax on an assumed income would be a restriction on the right to carry on the business besides being arbitrary.

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 asses-

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sing authority to ascertain whether the payment was genuine or whether it was out of the income from disclosed sources. The terms of Section 40A(3) are not absolute. Consideration of business expediency and other relevant factors are not excluded. The 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 the business transactions and to prevent the use of unaccounted money or reduce the chances to use black-money for business transactions. See: *Mudiam Oil Company v. ITO*, [1973] 92 ITR 519 A.P. If the payment is made by a crossed cheque drawn on a bank or a crossed bank draft then it will be easier to ascertain, when deduction is claimed, whether the payment was genuine and whether it was out of the income from disclosed sources. In interpreting a taxing statute the Court cannot be oblivious of the proliferation of black-money which is under circulation in our country. 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.

As to the second question it may be stated 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 all outgoings are brought under the word 'expenditure' for the purpose of the Section. The expenditure for purchasing the stock-in-trade is one of such outgoings. The value of the stock-in-trade has to be taken into account while determining the gross profits under section 28 on principles of commercial accounting. The payments made for purchases would also be covered by the word 'expenditure' and such payments can be disallowed if they are made in cash in the sums exceeding the amount specified under section 40A(3). We have earlier observed that Rule 6DD has to be read along with Section 40A(3). The Rule also contemplates payments made for stock-in-trade and raw materials. This Rule is in accordance with the terms of Section 40A(3). The Rule provides that an assessee can be exempted from the requirements of payment by crossed cheque or a crossed bank draft where the purchases are

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made of certain agricultural or horticultural commodities or from a village where there is no banking facility. Section 40A(3) is, therefore, attracted to payments made for acquiring stock-in-trade and other materials. This is also the view taken by several High Courts. See' *Sajowanlal Jaiswal v. CIT*, [1976] 103 ITR 706 Orissa; *U.P. Hardware Store v. CIT*, [1976] 104 ITR 664 Allahabad; *Ratan Udyog v. ITO*, [1977] 109 ITR 1 Allahabad; *P.R. Textiles v. CIT*, Kerala, [1980] 121 ITR 237 Kerala; *CIT, v. Kishan Chand Maheswari Dass*, [1980] 121 ITR 232 P & H; *Kanti Lal Purshottam and Co. v. CIT*, [1985] 155 ITR 519 Raj; *CIT, v. New Light Tin Mfg. Co.*, [1980] 121 ITR 229 P & H; *Fakri Automobiles v. CIT*, [1986] 160 ITR 504 Raj; *Venkata Satayanarayana Timber Depot v. ITR*, [1987] 165 ITR 253 AP.; and *Akash Films v. CIT*, [1991] ITR 32 Karnataka. The decisions of the High Courts of Andhra Pradesh, Orissa, Allahabad, Kerala, Karnataka, Punjab & Haryana, Rajasthan and Patna are to the effect that the payments made for purchasing stock-in-trade or raw materials should also be regarded as expenditure for the purpose of Section 40A(3). The only discordant note struck on this aspect is by the Gauhati High Court in *CIT v. Hardware*

Exchange, [1991] 190 ITR 61. The Gauhati High Court has observed that Section 40A(3) applies only to payments made on account of 'expenditure incurred' and the payment made purchase of stock-in-trade cannot be termed as 'expenditure incurred' since money does not go irretrievably in such cases. We are unable to agree with the view taken by the Gauhati High Court.

In this view of the matter we dismiss all these appeals and special leave petition with costs.

S.B.
dismissed.

Appeals

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JUDIS