



Global Business Tax Alert Sharp Insights

¹Calcutta High Court denies addition of waived interest income even where the taxpayer maintains accounts on mercantile basis

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¹ M/s. Shivlaxmi Exports Ltd. v. Commissioner of Income-tax [ITA No. 134 of 2001]

Background/ Facts

- Shivalxmi Exports Ltd. ('the taxpayer') advanced loans to two borrowers during the financial year 1985-86.
- The borrowers requested the tax payer not to charge any interest on the sums advanced, pursuant to which the taxpayer passed Board resolutions acceding to the request of the borrowers.
- The taxpayer in accordance with the resolution, did not charge any interest with respect to these two borrowers in the books of accounts.
- The Assessing Officer ('AO'), taking into view that the taxpayer follows mercantile system of accounting, added notional interest on the basis of the prevailing market rates.
- The Commissioner of Income Tax (Appeals) and the Tribunal upheld the position taken by the AO on the grounds that as the taxpayer maintained mercantile system of accounting, the debts were not declared as bad debts and the taxpayer continued to receive back the principal sums from the borrowers.

Ruling of the High Court

- The High Court observed that the taxpayer's decision to waive interest was based on commercial consideration.
- The High Court found that the interest income could not said to have accrued for the taxpayer in view of the resolutions taken for waiver of loan. The earlier decisions² of Apex Court laying down principles of taxability on the basis of real income was also taken on record.
- Further the Hon'ble High Court also distinguished the judgement of the Apex Court in the case of Shiva Prakash³ by observing that the facts in present case did not establish any linkage or nexus between the taxpayer and the two borrowers.

² Commissioner of Income tax vs. Birla Gwalior Pvt. Ltd. [(1973) 89 ITR 266 (SC)]; CIT vs. Shoorji Vallabhdas & Co. [(1962) 46 ITR 144] and Poona Electric Supply Co. Ltd. vs. CIT [(1965) 57 ITR 521]

³ Commissioner of Income tax vs. Shiv Prakash Janak Raj and Co. Pvt. Ltd. [(1996) 222 ITR 583]

Conclusion

The Hon'ble High Court reiterated the concept of notional income vis-à-vis real income. It held that no income could be said to have accrued where the decision of waiver of interest was taken on the basis of commercial expediency, backed by Board resolutions passed by the taxpayer.

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