UNREPORTABLE

* IN THE HIGH COURT OF DELHI AT NEW DELHI

\+ ITA No. 44 of 2008

% *Reserved on : July 13, 2009*
Pronounced on : July 24, 2009

Commissioner of Income Tax . . . Appellant

through : Mr. Subhash Bansal, Advocate

VERSUS

Sahib Chits (Delhi) (Pvt.) Ltd. . . . Respondent

through : Mr. Prakash Kumar, Advocate

CORAM :-
THE HON'BLE MR. JUSTICE A.K. SIKRI
THE HON'BLE MR. JUSTICE VALMIKI J. MEHTA

1. Whether Reporters of Local newspapers may be allowed to see the Judgment?
2. To be referred to the Reporter or not?
3. Whether the Judgment should be reported in the Digest?

A.K. SIKRI, J.

1. This appeal has been preferred under Section 260A of the Income Tax Act, 1961 (hereinafter referred to as 'The Act') against the order of the ITAT, New Delhi passed in ITA No. 857/Delhi/2006 on 4th May 2006 for the financial year 2003-04.

2. The assessee is a chit fund company. During the financial year under consideration it was running various chits. An on the spot verification was conducted on 21.12.05 at the business premises of the assessee and after collecting further details it was held by Assessing Officer

to its members on the chits contributed by them under vari organized by the assessee. While passing order under Section 201/201(1A) the AO quantified the default at Rs. 8, 17,683/- including tax (TDS), surcharge and interest payable by it.

3. In appeal, the action of the AO was quashed by the learned CIT(A) following the decisions in the below mentioned cases:

a) ***Sh. Ram Chit (P) Ltd.*** v. ***DCIT***, 83 ITD 792
b) ***Baldeep Singh*** v. ***Union of India***, 199 ITR 628
c) ***Shriram Chits & Investment (P) Ltd.*** v. ***Union of India & Ors.***, AIR 1993 SC 2063 (2074).

Besides the aforementioned, the learned CIT(A) has also relied on Para 4 of the CBDT Circular No. 647 dated 22.3.1993. The ITAT affirmed the aforesaid orders of the CIT (A) while dismissing the appeal of the Revenue.

4. The following substantial questions of law have been raised before us for our consideration :-

(a) Whether the ITAT was correct in law in holding that the assessee had not paid any interest to the subscribers of the chit and such payment does not fall within the meaning of interest as defined under Section 2(28A) of the Act?

(b) Whether the ITAT was correct in law in holding that the assessee was not required to deduct the tax at source within the meaning of Section 194A of the Act and as such the assessee

5. Since the assessee is a Chit Fund company, various subscribers become members of different chits which are floated by such a company. Normally, these chits are for a fixed period of 20, 25, 30 or 40 months. If the chit is for a period of 25 months, 24 members are made as subscribers and one chit remains with the organizer (i.e. the assessee herein) named as *'Foreman'*. The subscribers contribute fixed amount, every month, which is involved in the chit. Normally, 1st, 2nd or 3rd month's chit is taken by the *Foreman*. Thereafter, for subsequent chits, bids between the members take place. The person who gives the highest bid is entitled to take a particular chit. The amount of bid offered by him is distributed between the members/ subscribers. These chits are governed by the law known as the Madras Chit Funds Act, 1961, which is extended to the Union Territory of Delhi. As per the provisions of this Act, there is a restriction to make a bid upto 35% of the maximum value of the chit. If more than one person offered 35%, then between them chit is allocated to a person by a draw of lot. The bid amount offered by the successful bidder is then distributed equally among all the members. It is this amount which is paid to the members that is treated as *'interest'* by the Assessing Officer. On this premise, the Assessing Officer proceeded and opined that before disbursing this amount of *'interest'* to the members/subscribers, the assessee was required to deduct tax at source under Section 194A of the Act and

held that for not doing so it committed default and, therefo[re] liable for interest and penalty under Section 201/201(IA) of the Act.

6. The assessee disputed the aforesaid approach of the Assessing Officer as the contention of the assessee was that what is distributed to the members is not *'interest'* and, therefore, no deduction was required to be made under Section 194A of the Act. In this backdrop, the moot question which arises for consideration is as to whether payment of the aforesaid nature disbursed to the subscribers of the chit would amount to *'interest'* as defined under Section 2(28A) of the Act. If it is not *'interest'*, question of deduction of tax at source under Section 194A of the Act would not arise and, thus, the assessee would not be treated to be in default under Section 201 of the Act. Therefore, answer to question No. (b) would automatically be answered while deciding question No.(a) formulated above.

7. Before we proceed to examine the question No. (a), the relevant provisions, i.e., the sections in question of the Act, may be stated for a better understanding of the issues at hand :-

> "**Section 2(28A)**: 'interest' means interest payable in any manner in respect of any moneys borrowed or debt incurred (including a deposit, claim or other similar right or obligation)and includes any service fee or other charge in respect of the moneys borrowed or debt incurred or in respect of any credit facility which has not been utilised."

xx xx xx

> "**Section 194A: Interest other than interest on securities.**

income by way of interest other than income by way interest on securities, shall, at the time of credit of such inc to the account of the payee or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax thereon at the rates in force…"

8. A bare reading of Section 2(28A) of the Act would reveal that interest is payable in respect of *'moneys borrowed'* or *'debt incurred'*. It, of course, would include a deposit, claim or other similar right or application of any service fee or other charges in respect of the moneys borrowed or debt incurred. We have already disclosed the nature of transaction. All the subscribers/members of the chit contribute moneys each month and bid takes place among the members. The highest bidder is entitled to take the chit, i.e. the money contributed by all the members, after deducting the bid amount offered by him. It is this bid amount which is distributed among all the subscribers/members equally. Obviously, this amount is not in respect of any moneys borrowed by the assessee or any debt incurred by the assessee.

9. It is at this juncture that it is important to note that as per The Madras Chit Funds Act, 1961, as extended to the Union Territory of Delhi (Madras Act 24 of 1961), the term "dividend", and not "interest", has been defined to mean –

> "the share of a subscriber in the discount available under the chit agreement for ratable distribution among the subscribers at each installment of the chit".

10. The question raised before us is with regard to the taxability of the

such subscribers and not "dividend". Thus, it may be noted term *'interest'*, as defined under the Act, specifically speaks of "moneys borrowed or debt incurred (including a deposit, claim or other similar right or obligation)…". In the present case various persons are contributing to chits, which amount is taken by the successful bidder who offers certain discount. Further, it was observed in ***Shriram Chits & Investment (P.) Ltd.*** (supra) that:

> "…it would not be correct to state that each subscriber lends money to the person who gets chit earlier. It cannot also be construed that the person who gets chit later should be treated as the money lender. The agreement between the parties that is entered as per Section 6 of the Act, only provides for distribution of the chit amount…"

The Supreme Court further relied on the judgment of the Kerala High Court in ***Janardhana Mallan and Ors.*** v. ***Gangadharan and Ors.***, AIR 1983 Ker 178, wherein it was observed that on entering into the chit agreement a debt is not incurred by the subscriber for the amount of all the future installments and in respect of such amount there is no debtor-creditor relationship.

11. From the above it is clear that a chit agreement clearly does not fall within the ambit of "money lending" or "debt incurred" and, therefore, will not be covered by the definition of "interest" as contemplated by the Act.

12. To understand the meaning of the term *'interest'*, we may also refer to law dictionary and provisions contained in other enactments.

"Advantage or profit, esp. of a financial nature; a legal shar something; all or part of a legal or equitable claim to or r in property."

Likewise, the Interest Tax Act, 1974 defines interest to mean –

> "interest on loans and advances made in India and includes - (a) commitment charges on unutilized 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, but does not include – (i) interest referred to in sub-section (1B) of section 42 of the Reserve Bank of India Act, 1934 (2 of 1934); (ii) discount on treasury bills."

13. We may point out at this stage that the order of the Assessing Officer proceeds on the basis as if the contribution given by the subscribers/members every month amounts to deposit with the chit fund company, i.e. the assessee, and on that basis he proceeds as if the assessee is working as a banker and, therefore, the amount of bid disbursed equally among members is to be treated as *'interest'* payable on money borrowed. This approach is fallacious on the face of it and particularly in view of the principle laid down in the aforesaid judgment of the Supreme Court in ***Shriram Chits & Investment (P) Ltd.*** (supra) wherein the Apex Court observed that the subscriptions received from the members of the chit fund company in terms of contract are not treated as *'deposits'* for the purpose of Reserve Bank of India's directions. The amount contributed by the members every month is given back to them in the following manner - The successful bidder takes the entire amount *(minus)* the bid amount and the bid amount is disbursed equally among the members. Therefore, by no stretch of imagination the

'deposit' with the company, much less money borrowed by the assessee. The Assessing Officer also ignores an important fact that no person can do the business of banking without the necessary approval of license from the Reserve Bank of India under the Banking Regulation Act, as pointed out above. The chit fund operations are regulated statutorily by the Madras Chit Fund Act, as extended to Delhi, which have nothing to do with the banking business.

14. Thus, from whatever angle the matter is to be looked into, the amount disbursed to the members from their contribution cannot be treated as *'interest'*. The Tribunal was, thus, right in holding that the assessee had not paid any interest to its subscribers of the chit. This issue is, thus, decided against the Revenue and in favour of the assessee, affirming the order of the Tribunal in this behalf.

15. The second issue is with respect to the applicability of section 194A of the Act to the assessee's case. As pointed out above, the payments made/disbursed to the subscribers/members was not *'interest'* and, therefore, the question of deducting any tax at source therefrom would not arise. The ITAT has rightly held that the assessee was not required to deduct the tax at source within the meaning of section 194A of the Income Tax Act and as such the assessee was not in default under section 201 of the Act. We are in agreement with the ITAT as well as the CIT(A) to the extent that interest can only be

the case of a chit fund there is no borrowing of moneys nor a
is incurred and as such the provisions of section 2(28A) are not attracted. It is also clear that dividend/discount cannot be mistaken for interest income in the hands of the subscribers and therefore there has been no default under section 194A of the Act.

16. No substantial question of law arises. The appeal is, therefore, dismissed.

(A.K. SIKRI)
JUDGE

(VALMIKI J. MEHTA)
JUDGE

July 24, 2009
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