(6) In view of our decision in *Ved Parkash Bhatia's case* (supra), the counsel for the assessee cannot be permitted to raise the question of vires in reference proceedings, as we have no jurisdiction to go into the question of the legislative competence, and we have to decide the question referred, considering the provisions as applicable to the case and if the assess is keen to challenge the legislative competence that he can do only in a writ petition under Article 226 of the Constitution of India and not in reference.

(7) For the reasons recorded above, we answer the question in favour of the Revenue, that is, in the negative, and hold that the value of the land as on 1st January, 1954 has to be taken into consideration for finding out the capital gains. However, there will be no order as to costs.

R.N.R.

Before : G. C. Mital and S. S. Sodhi, JJ.

HINDUSTAN STEEL FORGINGS, RAJPURA,—*Applicant.*

versus

COMMISSIONER OF INCOME TAX, PATIALA,—*Respondent.*

Income Tax Reference No. 43 *of* 1981

March 2, 1989.

Income Tax Act (XLIII of 1961)—Ss. 37, 40(*b*)—*Deduction—Interest on deposits—Interest paid by the firm to partners on deposit on behalf of their H.U.F.—Interest paid—Whether can be rightly allowed as permissible deduction under S.* 40(*b*).

Held, that in view of Para 2 and sub-para (b) of the circular issued by the Central Board of Direct Taxes and printed in the statute Section of 149 I.T.R. at page 127, under the heading "Reducing litigation" makes the matter absolute. We are of the opinion that the Tribunal erred in law in disallowing interest under S. 40(b) of the Act to the three individuals who were partners not in their individual capacity but on behalf of H.U.F. as *Kartas*. Hence it has to be held that the interest paid is permissible deduction under S. 40(b) of the Act.

(Paras 2 to 4).

C.I.T. *v.* Nitro Phosphetic Fertilizer (1988) 174, I.T.R. 269.

Sanghi Motors *v.* C.I.T. Delhi (1982) 135 I.T.R. 359.

C.I.T. Karnataka (Central). *v.* Khoday Eswarsa and Sons (1985) 152 I.T.R 423.

Chandmul Rajgarhia *v.* C.I.T. (1987) 164 I.T.R. 486.

(Dissented from).

Reference under Section 256(1) *of the Income-tax Act,* 1961 *by the Income-tax Appellate Tribunal (Chandigarh Bench) to the Hon'ble High Court of Punjab and Haryana for opinion of the following question of law arising out of the Tribunal's order, dated* 3rd *October,* 1980 *in R.A. No.* 141/*Chd./*80 *in ITA No.* 436/79 *Assessment year* 1978-79:—

> *"Whether, on the facts and circumstances of the case, the Tribunal erred in law in disallowing under section* 40(b) *of the Income-tax Act,* 1961 *interest aggregating to Rs.* 12,840 *paid by the firm to three individuals who were partners on behalf of their HUFs as Kartas, on their deposits."*

B. S. Gupta, Sr. Advocate with Sanjay Bansal, Advocate, *for the applicant.*

Ashok Bhan, Sr. Advocate with Ajay Mittal, Advocate, *for the respondent.*

JUDGMENT

Gokal Chand Mital, J.

(1) Chiranji Lal, Mangat Rai and Jiwan were partners of M/s Hindustan Steel Forgings, Rajpura, the assessee, in their capacity as Kartas of their respective H.U.Fs. They had their personal accounts with the assessee in which they had advanced money in their individual capacity and during the accounting period, relevant to the assessment year 1978-79, the assessee paid interest to them on their individual accounts totalling Rs. 12,840. Before the Income Tax Officer, the assessee claimed deduction of the interest paid but the Income Tax Officer disallowed the same on the ground that it was hit by the provisions of section 40(b) of the Income Tax Act, 1961 (hereinafter called the Act) because the representative capacity of the partners could not be taken note of and the interest paid

would be considered as having been paid to partners. The Appellate Assistant Commissioner agreed with the Income Tax Officer and so also the Tribunal. On the aforesaid facts, the Income Tax Appellate Tribunal, Chandigarh, has referred the following question for opinion:—

> "Whether, on the facts and circumstances of the case, the Tribunal erred in law in disallowing, under section 40(b) of the Income Tax Act, 1961, interest aggregating to Rs. 12,840 paid by the firm to three individuals who were partners on behalf of their H.U.F.s. as Kartas, on their deposits ?"

(2) Section 40(b) of the Act as it stood in the assessment year, was interpreted by different High Courts on similar facts and there were divergent opinions. By insertion of explanations to the provision by the Taxation Laws (Amendment) Act, 1984, which came into force with effect from 1st April, 1985, and as a result of explanation 2, clause (i), it was provided that interest paid by the firm to an individual or by an individual to the firm otherwise than as a partner in a representative capacity shall not be taken into account for the purpose of clause (b). It is undisputed that if after 1st April, 1984 the interest is paid by an assessee firm to an individual, who is partner in the assessee firm as Karta of his H.U.F., then section 40(b) would not apply and the assessee firm would be entitled to claim deduction under section 37 of the Act. The aforesaid amendment was taken notice of by the Central Board of Direct Taxes and it issued a circular which is also found printed in the statute section of 149 I.T.R. at page 127. Under the heading "Reducing litigation", para 2 and sub-para (b) are relevant for reproduction :—

> "2. A number of amendments have been made to bring out the legislative intention more clearly so that further controversy and litigation regarding the true intent and purport of these provisions is avoided. To illustrate:
>
> (b) It has also been clarified that where a person is a partner in his representative capacity, interest paid to him in his individual capacity will not be disallowed under the above-mentioned provisions and *vice versa*."

(3) It is not disputed in view of the authoritative decision of the Supreme Court that such like circulars are binding on the department and the assessees are free to take benefit of the same. A reading of para 2 shows that by the amendment, the Legislature intended to state the law more *clearly* (underlined to put emphasis) so that further controversy and litigation regarding the *true intent and purport* (underlined to put emphasis) of these provisions is avoided. To illustrate the meaning of para 2 three illustrations were added and the relevant for us is illustration (b). A reading of the same shows that the amendment has clarified that where a person is a partner in his representative capacity, interest paid to him in his individual capacity, will not be disallowed under the above mentioned provisions and *vice versa*. Therefore, it is clear that the amendment brought in by the Amendment Act, 1984, was only clarificatory with a view to explain what was hidden so as to make it apparent to the naked eye. Such an amendment is always considered retrospective so that what looked hidden hitherto before should be considered as apparent and if that is so, the clarification which has been brought about by the amendment, should be read as if the unamended provision was also to be read in the same way and if that is so, the rulings which interpreted section 40(b) before the amendment to mean that the position of an individual in his individual capacity and that individual representing H.U.F. as a Karta, were two separate known legal entities for the purpose of Income Tax Law as also for the purpose of 'person' as defined in section 2(31) of the Act. Even in the definition of 'person' H.U.F. is a distinct entity as compared to an individual. By the amendment and particularly in view of the circular issued by the Central Board of Direct Taxes, the decisions of the High Courts, which are in consonance with the amended provision, were accepted so that the provision, as it existed before the amendment, was to be read in the light of the amended provision. Similar view has been taken by a Full Bench of Madhya Pradesh High Court in *C.I.T.* v. *Narbharam Popatbhai and sons* (1), and we fully agree with the same.

(4) Full Bench of Gujrat High Court in *Chhotalal and Co.* v. *C.I.T., Gujrat* (2), has also taken the same view without the aid of circular issued by the Central Board of Direct Taxes. Decisions of High Courts of Andhra Pradesh, Bombay, Madras and Rajasthan,

(1) (1987) 166 I.T.R. 534.
(2) (1984) 150 I.T.R. 276.

were also cited before us, taking the same view as that of the Full Bench of the Gujarat High Court and since all the aforesaid decisions are mentioned in the Full Bench decision of the Madhya Pradesh High Court, we are not discussing them in detail and following all these judgments, which are in line with our thinking, we disagree with the view taken to the contrary by the Allahabad High Court in its majority decision in *C.I.T.* v. *Nitro Phosphetic Fertilizer* (3), and rather approve the minority decision. We also dissent from the decisions of the Delhi High Court in *Sanghi Motors* v. *C.I.T., Delhi* (4), Karnataka High Court in *C.I.T., Karnataka (Central) v. Khoday Eswarsa and sons* (5), and Patna High Court in *Chandmal Rajgarhia v. C.I.T.* (6). The circular issued by the Central Board of Direct Taxes has made the matter easier otherwise we would have given a larger number of illustrations to show that even in the unamended provision of section 40(b) interest paid to a partner in one capacity, could not be confused with another capacity of the recipient of the interest. Only one such illustration is being noticed to highlight the point. A trust deposits the amount with a firm in which 'A' is a partner. Undisputably the interest would be an allowable deduction. Later on, 'A' becomes a Trustee. Could it be said under the unamended law that the interest will be disallowed as one of the Trustees was a partner in the assessee firm? The answer is 'no', because the Trust is a separate person and has a sparate legal entity as compared to 'A' who has two capacities—one as an individual and the other as a Trustee. Accordingly, we are of the opinion that the Tribunal erred in law in disallowing interest under section 40(b) paid to three individuals, who were partners not in their individual capacities, but on behalf of their H.U.F's. as Kartas. The referred question is answered in favour of the assessee in the affirmative, with no order as to costs.

R.N.R.

(3) (1988) 174 I.T.R. 269.
(4) (1982) 135 I.T.R. 359.
(5) (1985) 152 I.T.R. 423.
(6) (1987) 164 I.T.R. 486.