

Indian Banks' Association, Bombay and Others v. M/s. Devkala Consultancy Service and Others

Civil Appeal No. 4655 of 2000 with Civil Appeal No. 5218 of 2000

[2004] Supp. 1 SCR 225 | 2004-04-16

Interest-tax pass-through: section 26C did not authorise grossing-up and upward rounding of loan interest

Interest-tax Act, 1974: sections 2(5), 2(7), 4, 5, 6 and 26C | Banking Regulation Act, 1949: section 35A | Constitution of India: Articles 12, 32, 226, 265 and 366(28)

Two-judge Bench; judgment delivered by S. B. Sinha, J. | V. N. Khare, CJI | S. B. Sinha, J.

Historical Interest-tax Act decision

The judgment concerns section 26C and the challenged historical tax pass-through. Do not use its 3% tax illustration as a current tax rate or treat it as a general prohibition on all contractual bank-interest revisions.

Remedy was a fund, not universal individual refunds

Although the Court recognised excess recovery from borrowers, it directed recovery into a fund for persons with disabilities, with additional Rs. 50 lakh contributions from each appellant and other concerned bank. It did not direct immediate individual refunds to every borrower.

Internal report-date discrepancy

The procedural introduction and SCR p. 233 identify the Karnataka High Court judgment as 18 December 1998; the opening judicial paragraph on SCR p. 231 prints 18 December 1994. The Supreme Court caption date of 16 April 2004 is clear. This note does not silently resolve that internal discrepancy.

01 FACTS OF THE CASE

Following the 1991 reintroduction of interest-tax, RBI advised scheduled commercial banks that the incidence should be passed pro rata to borrowers using a uniform practice. Indian Banks' Association proposed loading interest with the 3% tax and rounding to the next higher quarter percentage point; RBI approved the proposal in 1993. A chartered-accountant firm challenged the resulting excess recovery in public-interest proceedings. The Karnataka High Court held the upward rounding illegal and directed accounting and deposit of the excess. The banks contended that iterative grossing-up and rounding preserved contractual interest after tax, reflected practical calculation difficulties and were authorised by RBI. They also challenged the petitioner's standing and maintainability. A connected appeal was brought by the Association of Borrowers of Karnataka. The Union of India opposed the banks' computation and acknowledged that portions of the excess had reached both banks and Government.

Source: [Background, High Court order and parties' submissions / PDF pp. 7-12](#)

02 DISCUSSION BY THE HON'BLE COURT

Section 26C was an enabling provision for passing on only the interest-tax legally payable in relation to the term-loan interest; it did not authorise an additional profit through tax recovery. The Court held that chargeable interest had to be calculated first, by reference to the contractual rate, before passing on the tax incidence. The banks' repeated addition of tax to the interest base and upward rounding rested on an erroneous premise. In the Court's historical illustration, Rs. 100 lent at 10% produced Rs. 10 interest and a borrower payment of Rs. 10.30, not Rs. 10.50. Articles 265 and 366(28) required legal authority for recovery as tax or its equivalent. The banks had acted under the statutory pass-through, not an independently exercised contractual revision power. RBI's approval under banking powers could not enlarge the Interest-tax Act. The Court rejected de minimis: small amounts per borrower aggregated into substantial unjust enrichment. It also accepted the chartered-accountant firm's standing, given its subject knowledge and the public injury, distinguishing an informed public-interest petitioner from a mere busybody.

Source: [Statutory construction, standing and RBI authority / PDF pp. 15-25](#)

03 JUDICIAL DECISION

The Court held the challenged grossing-up and rounding illegal and the purported RBI approval without jurisdiction and ultra vires the Interest-tax Act. Section 26C could override earlier term-loan agreements only to the extent of the legally payable interest-tax burden. Practical difficulty, a small individual excess or the language of contractual interest could not validate the particular statutory recovery. The High Court's conclusion on illegality was upheld. The Court distinguished earlier banking and contract decisions; its reasoning did not displace RBI's lawful directions generally or decide that every independently authorised interest revision was impermissible.

Source: [Holding on section 26C and limits of RBI approval / PDF pp. 17-25](#)

04 OUTCOME / IN WHOSE FAVOUR

Both appeals were dismissed on the stated terms, without costs. Recognising the difficulty of monitoring refunds across more than five crore borrowers, the Court directed creation of a fund for persons with disabilities. It requested the Comptroller and Auditor General of India to recover the excess realised by the Union of India as interest-tax and by banks and financial institutions as interest, forming the fund's corpus. Each appellant and other concerned bank was also directed to contribute Rs. 50 lakh. The CAG would chair the trust, with the Union Finance Secretary and Law Secretary as ex-officio members; the Union, RBI, banks and financial institutions were to cooperate. Trustees could frame a scheme and seek further directions. The order contemplated transfer of the corpus to a future statutory authority if legislation provided one. This note reports those directions without asserting their later implementation.

Source: [Fund, bank contributions, trustees and operative dismissal / PDF pp. 29-30](#)

05 AKHB REVIEW POINT

AKHB analysis: distinguish the taxpayer's statutory liability, the legal authority to transfer its burden, and the amount actually recovered from customers. Test any tax-labelled surcharge against the precise enabling provision and underlying computation; administrative approval does not supply missing statutory authority. An apparently small recurring excess can be material across an entire borrower population. Preserve the remedial distinction: success on illegality does not itself establish an individual refund mechanism. A present claim requires the applicable enactment and contract, the relevant period, evidence of recovery, limitation and subsequent orders to be checked. The judgment's recognition of an informed chartered-accountant firm's public-interest standing was fact-specific and is not a general licence to initiate any unrelated PIL.

Source: [Primary reasoning underlying AKHB analysis / PDF pp. 16-25](#)

SOURCE & VERIFICATION

Supreme Court Reports scan - public eSCR mirror

The complete 30-page report was read. The reporter's headnote occupies SCR pp. 225-231 / PDF pp. 1-7. Judicial reasons begin on SCR p. 231 / PDF p. 7 and conclude on SCR p. 254 / PDF p. 30. The report includes submissions, quoted statutes and earlier judgments that must not be confused with the Court's own holdings. No adjoining case is included.

Open cited source rendition

The downloaded 30-page source exactly matches catalogue SHA-256
2d0fba7e9de70890ede96a2dac542eb38329f85f496243a7226d6943061a0e9c.

All text was read in contiguous, untruncated PDF ranges 1-8, 9-16, 17-24 and 25-30; the operative fund directions and dismissal were read on PDF pp. 29-30.

Published corpus searches found no matching Devkala/Indian Banks' Association identity, Civil Appeals 4655 or 5218 of 2000, or exact source hash. The source catalogue entry is this pending asset, not another publication.

Interest-tax Act merits coverage is already represented by Ratnakar Bank, IDBI, ICICI Bank, City Union Bank, State Bank of Patiala and Muthoot notes. This source has substantive Interest-tax Act interpretation and is not included merely because it mentions income tax.

The annual recovery figure on SCR p. 232 appears as an allegation in the litigation history; it is not treated as an audited quantum finding.

The internal High Court date discrepancy is disclosed, not silently corrected. The Supreme Court date, Bench and both appeal numbers are clear in the source.

STATUTORY SCOPE

This is a historical Interest-tax Act, 1974 decision concerning the tax pass-through following the 1991 reintroduction and the then section 26C. The tax rates and numerical illustration are historical. It is not a present rule for pricing loans or a finding that every contractual interest revision is unlawful. Present statutory applicability and subsequent judicial treatment have not been comprehensively verified.

LATER TREATMENT

Source checked 2026-10-12. No comprehensive later-treatment or current-law check has been completed. The directions are reported as made on 16 April 2004; later administration, implementation or modification of the fund directions has not been verified.

Related note: [The Commissioner of Income Tax, Kolhapur v. The Ratnakar Bank Ltd.](#)

Related note: M/s. State Bank of Patiala through General Manager v. Commissioner of Income Tax, Patiala

AI DISCLOSURE

This AKHB research note was prepared with AI assistance from the identified primary source; independent human review is not represented.

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General legal and tax research only; not legal or tax advice. Verify the complete judgment, applicable statutory version and subsequent judicial treatment before reliance. The AKHB REVIEW POINT is editorial analysis, not the Court's holding. No current-law clearance is claimed.