
(1986) 09 CAL CK 0010

In the Calcutta High Court

Case No : Income-tax Reference No. 828 of 1979

Commissioner of Income Tax

APPELLANT

Vs

Agarpara Co. Ltd.

RESPONDENT

Date of Decision : 17-09-1986

Acts Referred:

Income Tax Act, 1961 — Section 37(2B)

Citation : (1987) 59 CTR 155 : (1987) 167 ITR 866 : (1987) 30 TAXMAN 359

Hon'ble Judges : Monjula Bose, J;Dipak Kumar Sen, J

Bench : Division Bench

Advocate : M.L. Bhattacharyya, for the Appellant;R.N. Dutta, for the Respondent

Judgement

Dipak Kumar Sen, J.—On an application of the Revenue u/s 256(1) of the Income Tax Act, 1961, the Tribunal has referred the following questions, as questions of law arising out of its order, for the opinion of this court :

"1. Whether, on the facts and in the circumstances of the case, and on a correct interpretation of Section 37(2B) of the Income Tax Act, 1961, the Tribunal was correct in holding that the expenditure of Rs. 53,487 was an allowable expenditure in computing the profits and gains of the assessee's business ?

2. Whether, on the facts and in the circumstances of the case, the Tribunal was correct in holding that the amount of Rs. 48,440 representing "difference" paid for non-fulfilment of contract for supply of flour and cement bags was an allowable deduction in computing the total income for the assessment year 1972-73 ? "

2. So far as question No. 2 is concerned, the controversy raised therein is covered by the two decisions of this court in COMMISSIONER OF Income Tax, WEST BENGAL Vs. PIONEER TRADING COMPANY PRIVATE LTD., and Commissioner of Income Tax Vs. Ramjeewan Sarawgee and Sons., . The decision of this court in COMMISSIONER OF Income Tax, WEST BENGAL Vs. PIONEER TRADING COMPANY PRIVATE LTD., has been approved by the Supreme Court

Subsequently in Commissioner of Income Tax, Bombay City-III Vs. Shantilal P. Ltd., .

3. In view of the aforesaid, we answer question No. 2 in the affirmative and in favour of the assessee.

4. The facts relating to question No. 1 are, inter alia, that the Agarpara Co. Ltd., the assessee, was assessed to Income Tax in the assessment year 1972-73, the accounting year ending on March 31, 1972. After the assessment was completed, the Commissioner of Income Tax, West Bengal-V, initiated proceedings u/s 263 of the Income Tax Act, 1961, The Commissioner noted that in the said assessment year, the assessee had spent Rs. 53,487 on cigarettes and other items supplied to its customers and claimed deduction of the same under the head "general charges". The said claim was allowed by the Income Tax Officer in computing the total income of the assessee. It appeared to the Commissioner that the said amount was not allowable as deduction u/s 37(2B) of the Income Tax Act, 1961, being expenditure on entertainment, and, therefore, the assessment was prejudicial to the interests of the Revenue.

5. On a show-cause notice issued, the assessee appeared before the Commissioner and contended that the said expenditure on cigarettes and other items was incurred for its customers and such expenditure was incurred wholly and exclusively for the purpose of the business of the assessee. It was contended that the said expenditure was not on account of entertainment but to provide basic necessity or by way of ordinary courtesy according to the long-standing practice or custom of trade and business.

6. The Commissioner did not accept the contention of the assessee. He held that the expenditure was incurred for the purpose of business, but the same was not allowable as a deduction by reason of Section 37(2B) of the Act, as the said expenditure was on account of entertainment. He held, following a decision of the Allahabad High Court in Brij Raman Dass and Sons Vs. Commissioner of Income Tax, , that refreshment or gratification of all kinds supplied would come within the meaning of entertainment. The Commissioner directed the Income Tax Officer to disallow the said expenditure and modify the assessment accordingly.

7. Being aggrieved, the assessee preferred an appeal to the Income Tax Appellate Tribunal. The Tribunal noted its earlier decision in the case of the same assessee for the subsequent assessment year 1973-74, where the Tribunal had followed a decision of the Gujarat High Court in Commissioner of Income Tax, Gujarat II Vs. Patel Brothers and Co. Ltd., , and had held that the expenditure incurred by the assessee in providing cigarettes and other items to its customers was an expenditure incurred out of commercial expediency and to meet customary hospitality. The Tribunal set aside the decision of the Commissioner and restored the original assessment by the Income Tax Officer allowing deduction of the said amount.

8. The present reference was initiated from the above order of the Tribunal.

9. At the hearing, the learned advocate for the Revenue submitted that there was divergence of opinion between High Courts on the point involved. He submitted that other High Courts have followed the decision of the Allahabad High Court in *Brij Raman Dass and Sons Vs. Commissioner of Income Tax*, and have dissented from the view taken by the Gujarat High Court. Learned advocate relied on and cited the following decisions :

(a) *Brij Raman Dass and Sons Vs. Commissioner of Income Tax*, : In this case, expenditure had been incurred by the assessee for providing tea, lassi and other refreshments to its customers and a deduction of such expenditure was claimed. A Division Bench of the Allahabad High Court considered the meaning of the word "entertainment" from Stroud's Judicial Dictionary in connection with the Refreshment Houses Act, 1960, and found that entertainment would include provision of food, drinks and other items reasonably required for personal comfort of the guests. It was held that entertainment expenditure would include expenditure incurred in connection with the business of the assessee for the entertainment of its customers and constituents and such entertainment might consist of providing refreshments as also other forms of entertainments. It was held that the provision of refreshments to the customers by the assessee resulted in an expenditure in the nature of entertainment expenditure and came within the mischief of Section 37(2A) of the Income Tax Act, 1961.

(b) *Commissioner of Income Tax Vs. Veeriah Reddiar*, . In this case, the assessee carrying on business in piece-goods on wholesale and retail basis incurred expenses in supplying to its customers cigarettes, coffee and occasional meals. The assessee had claimed deduction in respect of the expenditure incurred in respect of the aforesaid in the relevant assessment year. The question was considered by a Full Bench of the Kerala High Court. The court noted the legislative history in respect of the allowability of such expenditure and considered the relevant Section of the Indian Income Tax Act, 1922, as also Section 37 of the Income Tax Act, 1961, and further Sub-sections (2A) and (2B) which were introduced in the said Section 37 by subsequent amendment. The court noted that in Sub-sections 37(2A) and 37(2B), the expression used was not entertainment expenditure but expenditure in the nature of entertainment. It was held that the expression used was much wider than the expression "entertainment expenditure" and included expenditure of allied nature having the characteristic of entertainment expenditure.

On a consideration of the dictionary meaning of the word "entertainment", the court came to the conclusion that the expression "entertainment expenditure" occurring in Sub-sections (2A) and (2B) of Section 37 of the Act should be taken to mean hospitality of any kind extended by an assessee directly in connection with his business. The court dissented from the view expressed by the Gujarat High Court in *Commissioner of Income Tax, Gujarat II Vs. Patel Brothers and Co. Ltd.*, , followed the decision of the Allahabad High Court in *Brij Raman Dass and Sons Vs. Commissioner of Income Tax*, and held that the expenditure incurred by

the assessee in supplying coffee, tea and other refreshments to its customers was expenditure in the nature of entertainment within the meaning of Section 37(2A) of the Act.

(c) Commissioner of Income Tax Vs. Khem Chand Bahadur Chand, . In this case, a Full Bench of the Punjab and Haryana High Court also considered the question whether expenditure incurred by an assessee in supplying food and drinks to its customers was in the nature of entertainment expenditure and came within the mischief of Section 37(2A) of the Act of 1961. The court considered the legislative history of the relevant provisions in respect of entertainment expenditure in the Indian Income Tax Acts as also the corresponding provisions in English law and came to the conclusion that it was the intention of the Legislature to disallow all expenditure in the nature of entertainment expenditure. The court also took note of the expression "in the nature of entertainment expenditure" and held that the said expression was wide enough to include all types of expenditure incurred on hospitality. It was held that the judgment of the Gujarat High Court and to other High Courts which had taken a contrary view did not consider the effect and the meaning of the wide expression. It was held that there was no reason to make a distinction between entertainment and hospitality in the manner in which it was done by the Gujarat High Court and to come to a conclusion that only where the hospitality was lavish or extravagant, the same could be held to be entertainment. It was observed that this distinction would make the application of the law difficult in individual cases. The court, however, noted that there may be cases where certain facilities like providing customers with drinking water would neither be entertainment nor hospitality and such cases might be excluded from the mischief of Section 37(2B) of the Act.

10. Learned advocate for the Revenue drew our attention to the other decisions which had taken the same view. The same were:

(a) Commissioner of Income Tax Vs. C.P.A. Yoosuf, , a decision of the Kerala High Court.

(b) Commissioner of Income Tax Vs. Manoo Ram Ram Karan Dass, , a decision of the Allahabad High Court.

(c) Commissioner of Income Tax Vs. Modi Spinning and Manufacturing Mills Co. Ltd., , a decision of the Allahabad High Court.

11. Learned advocate for the assessee contended, on the other hand, that apart from the Allahabad, Punjab and Kerala High Courts, the other High Courts including this court have taken a different view on the controversy. He submitted that, in the instant case, it has been found, as a fact, by the Tribunal that the expenditure in issue was incurred for supplying of items like cigarettes, etc., as a matter of ordinary courtesy and not by way of lavish entertainment. The total expenditure incurred was insignificant compared to the total business turnover of the assessee. He submitted further that the controversy stood concluded by the

Supreme Court when it refused to allow the SLP (Civil) No. 3781 of 1978 which was filed against an order of the Bombay High Court dismissing the application of the Commissioner of Income Tax u/s 256(2) of the Income Tax Act, 1961, in the case of CIT v. Allied Publishers Ltd. In that case, the expenditure incurred was on account of lunch supplied by the assessee to its up-country customers and had been allowed as a deduction. The allowability of the deduction had been sustained by the Bombay High Court.

12. Learned advocate submitted further that in Income Tax Reference No. 503 of 1979 (intituled CIT v. Howrah City Engineering Co. (P) Ltd.), in an unreported judgment dated June 14, 1984, this court followed the view taken by the Gujarat High Court and other High Courts following Gujarat and held that the expenditure incurred on refreshments supplied to customers was not in the nature of entertainment expenses.

13. Learned advocate for the assessee cited the following decisions :

(a) Commissioner of Income Tax, Gujarat II Vs. Patel Brothers and Co. Ltd., . In this case, a Division Bench of the Gujarat High Court considered the question of allowability of an expenditure u/s 37(2A) of the Income Tax Act, 1961. The court considered the meaning of the expressions "entertainment" and "hospitality" from a number of dictionaries and came to the conclusion that every act of entertainment included hospitality but every hospitality did not constitute entertainment. It was held that hospitality shown on account of business obligations arising as a result of express or implied contract or out of long-standing custom of a trade, business or profession did not amount to entertainment and such hospitality could not be included in and covered by the term "entertainment". The Gujarat High Court dissented from the view taken by the Allahabad High Court in Brij Raman Dass and Sons Vs. Commissioner of Income Tax, and held that if food or drinks were provided to a client, constituent or customer and was in the nature of bare necessity, or by way of ordinary courtesy, or an express or implied term of a contract of employment spelt out from long-standing custom, it would not amount to entertainment. But provision of food or drinks to a client, customer or constituent on a lavish or extravagant scale would be an entertainment per se. Provision of food or drinks to a client, customer or constituent in a liberal and friendly way might amount to entertainment.

(b) Commissioner of Income Tax, Vidarbha And Marathwada Vs. Shah Nanji Nagsi, . In this case, a Division Bench of the Bombay High Court took the same view as the Gujarat High Court in Commissioner of Income Tax, Gujarat II Vs. Patel Brothers and Co. Ltd., and held that where the assessee carrying on pakki adat business supplied messing and lodging to its constituents who came from outside for a limited time in its mess and also supplied tea and pan to its customers, the expenditure incurred was actually an essential part of the business and did not partake of the nature of hospitality or entertainment.

(c) Commissioner of Income Tax, Karnataka Vs. Corporation Bank Ltd., . In this case, a Division Bench of the Karnataka High Court held that the assessee, a banking company, which had incurred expenditure in supplying coffee and tea to its customers at its branches during business hours, was entitled to claim deduction of the same and such expenditure was not in the nature of entertainment expenditure. It was noted that the items supplied were not at any reception or a party and that there was no guest and host relationship between the assessee and its customers.

(d) Commissioner of Income Tax Vs. Karuppuswamy Nadar and Sons, . In this case, a Division Bench of the Madras High Court took the same view as the Gujarat High Court in Commissioner of Income Tax, Gujarat II Vs. Patel Brothers and Co. Ltd., and held that expenditure incurred by an assessee in supplying coffee and tea to its customers was not in the nature of entertainment and was allowable as deduction u/s 37. The court observed that it was a misnomer to call coffee or tea an item of entertainment.

(e) CIT v. Lakhmichand Muchhal [1982] 134 ITR 234. In this case, a Division Bench of the Madhya Pradesh High Court followed the decisions of the Gujarat High Court in Commissioner of Income Tax, Gujarat II Vs. Patel Brothers and Co. Ltd., and of the Bombay High Court in Commissioner of Income Tax, Vidarbha And Marathwada Vs. Shah Nanji Nagsi, and of the Andhra Pradesh High Court in Addl. Commissioner of Income Tax Vs. Maddi Venkataratnam and Co. Ltd., and held that expenditure incurred by an assessee in providing messing to its trade constituents by way of ordinary courtesy would not amount to an expenditure in the nature of entertainment as contemplated u/s 37(2B) of the income tax Act, 1961.

(f) Commissioner of Income Tax Vs. Supreme Motors (P.) Ltd., . In this case a Division Bench of the Delhi High Court took note of the divergent views of the High Courts on the controversy and held that where a small expenditure was incurred by the assessee for supplying tea and cold drinks to its customers, the same could not be held to be in the nature of entertainment expenditure. It was observed that it was a matter of degree and should not be stretched to the extent of disallowing petty claims.

(g) Santlal Kashmirilal Vs. Commissioner of Income Tax, Delhi, . In this case, another Division Bench of the Delhi High Court held that expenditure incurred by the assessee, carrying on the business of arhtias in foodgrains in Delhi, in supplying customary items of refreshment to its trade constituents, was a customary expenditure and was incurred as a part of the business operation and the same would be allowable as a deduction. The Division Bench took note of Explanation 2 which was introduced in Section 37(2A) of the Income Tax Act, 1961, by the Finance Act, 1983, with retrospective effect from April 1, 1976. The said Explanation reads as follows Commissioner of Income Tax, Tamil Nadu-V Vs. Workshop Trust, (See Santlal Kashmirilal Vs. Commissioner of Income Tax, Delhi,):

"Explanation 2.--For the removal of doubts, it is hereby declared that for the purposes of this sub-section and Sub-section (2B), as it stood before the 1st day of April, 1977, "entertainment expenditure" includes expenditure on provision of hospitality of every kind by the assessee to any person, whether by way of provision of food or beverages or in any other manner whatsoever and whether or not such provision is made by reason of any express or implied contract or custom or usage of trade, but does not include expenditure on food or beverages provided by the assessee to his employees in office, factory or other place of their work."

14. This amendment was made retrospective on and from April 1, 1976. Inasmuch as the expenditure, before the Delhi High Court, was incurred in the assessment years 1972-73 and 1973-74, it was held that the same did not come within the mischief of the explanation introduced by way of amendment.

15. On a consideration of the decisions cited before us, it appears that the controversy has now been set at rest by Explanation 2 introduced in Section 37(2A) of the Income Tax Act under the Finance Act 1983, noted hereinabove. In the instant case, the expenditure was incurred before April 1, 1976, the date on which, the new Explanation came into effect. Therefore, we have to consider the law as it stood before the incorporation of the said Explanation in Section 37(2A). It appears to us that the law as laid down by a number of High Courts recognised a distinction between entertainment and hospitality. The view taken by the Gujarat High Court in Commissioner of Income Tax, Gujarat II Vs. Patel Brothers and Co. Ltd., was that entertainment and hospitality connoted different ideas and that every act of hospitality would not amount to entertainment. With respect we agree with the said view. The same has been recognised in the new Explanation 2 which has been incorporated in Section 37(2A) by the Finance Act, 1983, In that view, the expenditure incurred by an assessee in rendering acts of hospitality to its customers as a common courtesy by way of supply of ordinary items of refreshments and other items like cigarettes, etc. cannot be held to be entertainment and the expenditure incurred for the said purpose cannot be held to be expenditure in the nature of entertainment. The meaning of the expression "expenditure in the nature of entertainment" cannot be stretched to include expenditure incurred for hospitality or expenditure in the nature of hospitality. The two concepts are different and their nature are also necessarily different.

16. In any event, we are bound by the decision of this court recorded in the judgment dated June 14, 1982 (sic) in Income Tax Reference No. 503 of 1979 which has been referred to earlier and has been relied on by the assessee. We also take note of the fact that the Supreme Court did not allow the SLP which was sought to be moved from a decision of the Bombay High Court on the same point.

17. For the reasons above, we answer question No. 1 in the affirmative and in favour of the assessee.

18. There will be no order as to costs.

Monjula Bose, J.

19. I agree.