

(2016) 08 KAR CK 0103

In the Karnataka High Court

Case No : I.T.A. Nos. 103-104 of 2011 with 155-156 of 2011, 343 of 2012, 70 and 71 of 2014 and 233 of 2015

Commissioner of Income-Tax

APPELLANT

Vs

G. Balraj

RESPONDENT

Date of Decision : 31-08-2016

Acts Referred:

Income Tax Act, 1961 — Section 40(a)(ia)

Citation : (2017) 390 ITR 50

Hon'ble Judges : Jayant Patel and S.N. Satyanarayana, JJ.

Bench : Division Bench

Advocate : Chythanya K.K, Advocate, for the Respondent; E.I. Sanmathi, Advocate, for the Appellant

Final Decision : Disposed Off

Judgement

Jayant Patel, J. - Considering the facts and circumstances of the case the first matter in chronology being I.T.A. Nos. 103-104 of 2011 when admitted, following substantial question of law was formulated by the court :

"Whether the finding of the Tribunal that the agreement between the assessee and Sri Bapuji is not a sub-contract, but it is joint venture, is contrary to material on record and based upon conjunctures and surmises and unsustainable ?"

2. Since this matter was admitted, the other matters of the present group are admitted. At the time of admission, the questions are differently framed but considering the facts and circumstances of the case, it appears to us that the above referred question would remain as common in all the matters and additionally one more question can to be formulated and the same is as to :

"Whether considering the facts and circumstances of the case section 40(a)(ia) of the Income-tax Act, can be made applicable or not ?"

3. Hence all the group of appeals needs to be considered on the basis of the

above referred to two questions.

4. The short facts are that the assessee is a Public Works Department (PWD) Contractor and as per the assessee, he has entered into agreement with Sri Bapuji Construction, whereby a particular percentage of the income of the contract is to be shared in different proportion. The assessee has shown his income to the extent of the amount received by it. However, in the assessment proceedings, the Assessing Officer found that as the TDS was deducted of the total amount of the contract (received by the assessee as well as by Sri Bapuji), the rest of the amount (amount of the contract minus the amount already shown in the return by the assessee) was disallowed and the same was added to the profit/income and the assessment order was passed. In the appeal before Commissioner of Income-tax (Appeals), it was held that the amount received by Sri Bapuji could not be assessed as the assessee's income and therefore the disallowance and the resultant addition in the income was deleted. In the appeal before the Tribunal in I.T.A. Nos. 103-104 of 2011 it was found by the Tribunal at paras. 6 to 9 as under :

"6. Having heard both the parties and having considered the rival contentions, we find that the only dispute is whether the agreement between the assessee and Sri Bapuji is a sub-contract or an agreement by which the income is diverted by overriding title. There is no dispute that the contract was awarded to the assessee and Sri Bapuji has executed the work awarded to the assessee. Having gone through the agreements between both the parties, it is observed that it is the assessee who has submitted the tender while it is Sri Bapuji who has deposited the requisite earnest money deposit (EMD). Both the parties have opened a joint bank account even prior to entering into agreement. It is also evident that Sri Bapuji is authorised to operate the said account. From these facts, it is to be examined if is diversion of income by overriding title or it is mere application of income. The learned Departmental representative had submitted that the Commissioner of Income-tax. (Appeals) had misconstrued the judicial precedent in coming to the conclusion that there is a diversion of income by overriding title. We have gone through the decisions quoted by the Commissioner of Income-tax (Appeals) and the oldest and most authoritative decision quote by him is in the case of CIT v. Sitaldas Tirathdas [1961] 41 ITR 367 (SC) wherein it has been observed that the true test of diversion of income by overriding title is whether the amount sought to be deducted, in truth, never reached the assessee as his income. Obligations no doubt there are in every case, but it is the nature of the obligation which is the decisive fact. There is a difference between an amount which a person is obligated to apply out of his income and an amount which by the nature of obligation cannot be said to be a part of the income of the assessee. Where, by the obligation, income is diverted before it reached the assessee, it is deductible ; but where the income is required to be applied to discharge an obligation after such income reaches the assessee, the same consequence in law does not follow. It is the first kind of payment which can truly be excused and not the second. The second payment is merely an

obligation to pay another a portion of one's own income which has been received and is since applied. The first is a case in which the income never reached the assessee, who even if he were to collect it, does so, not as part of this income, but for and on behalf of the person to whom it is payable.

6.1 Thus to apply the doctrine of diversion of income by overriding title, the first and foremost condition to be satisfied is the nature of the assessee's obligation, whether by the obligation, the income is diverted before it reaches the assessee, or whether the income is required to be applied to discharge an obligation after such income reaches the assessee. In the case before us, we find that the agreement is entered into by the parties even before the contract is awarded and the receipt can be appropriated by the second party even without any further approval from the assessee. Whether these factors can be said to determine the nature of the obligation ? In our opinion, they do not. The real determinative factor is the point at which the second party gets a right to receive the income. The agreement would be ineffective and non-executable unless and until the contract is awarded to the assessee and the same is executed in accordance with the terms and conditions of the contract. A perusal of the agreement between the assessee and Sri Bapuji shows that he is entitled to all the benefits of the contract but no obligation of the contract are fastened on to him. Thus, the obligation of the contract are still with the assessee and therefore, it cannot be said that the assessee was only lending his name whereas in the letter and spirit the contract is to be executed and the receipts enjoyed by Sri Bapuji. Therefore, as the contractor, the assessee is entitled to receive the contract receipts and it is thereafter that Sri Bapuji is entitled to receive the same. Thus, it is a clear case of application of income and not diversion of income by overriding title as held by the Commissioner of Income-tax (Appeals). In view of the same, the order of the Commissioner of Income-tax (Appeals) is set aside on this point. However, there is another angle to this issue. The assessee has only received commission from Sri Bapuji who has executed the contract. From the facts of the case detailed above, it looks like a joint venture from the inception and not a sub-contract. The agreement between the assessee and Sri Bapuji is prior to the award of the contract and both of them have opened a joint account to enable Sri Bapuji to appropriate the receipts. Thus it can be seen that it is more in the nature of a joint venture and is not a sub-contract. In such a case, the assessee would not be liable to deduct tax at source. As this angle of the issue has not been looked into by the authorities below, we deem it fit and proper to remand this issue to the file of the Assessing Officer a reconsideration in accordance with law.

7. The other grievance of the Revenue is that the Commissioner of Income-tax (Appeals) has granted relief to the assessee on the ground that when the assessee has not claimed the payment as expenditure, the provisions of section 40(a)(ia) could not be applied and the Assessing Officer could not have made the disallowance of the same. In support of his contention, the learned counsel for the assessee had placed reliance upon the decision of the Bangalore Income-tax

Appellate Tribunal in the case of Balaji Engineering and Construction Works v. Joint CIT (Asstt.) in I.T.A. Nos. 283 and 284/Bang/2002, dated November 15, 2002 wherein considering the disallowance under section 40A(3) of the Income-tax Act, 1961, it was held that the payment made to sub-contractors have not been claimed as a revenue expenditure and the appellant is merely acting as a conduit for channelising the contract amount received from the Government Departments to the sub-contractors, who have actually spent the amounts and therefore such payments do not have a revenue character and the provisions of section 40A(3) cannot apply. He also drew our attention to the decision of the hon'ble jurisdictional High Court in the case of CIT v. Balaji Engineering and Construction Works [2010] 323 ITR 351 (Karn), where the finding of the Tribunal was upheld.

8. The learned Departmental representative, on the other hand, submitted that the assessee ought to have considered all the receipts as his income and claimed the payment made to Sri Bapuji as deduction thereafter and the fact that entire tax deducted at source has been deducted from his payment proves that the contention of the assessee that it is not showing the receipts and not claiming the payment is not correct. As regards the decision relied upon by the assessee, he submitted that it relates to disallowance under section 40A(3) whereas the issue before us is with regard to disallowance under section 40(a) (ia) and therefore, the said decision is not applicable to the facts of the case before us.

9. Having heard both the parties, we find that the assessee has not claimed the payment to Sri Bapuji as revenue expenditure and has only offered the commission from the contract as his income. But, we have already held that the agreement between the assessee and Sri Bapuji, is not a sub-contract and is in the nature of a joint venture. Having held so, we proceed to consider the disallowance under section 40(a)(ia). Section 40(a)(ia) provides as under :

Notwithstanding anything to the contrary in sections 30 to 38, the following amounts shall not be deducted in computing the income chargeable under the head "Profits and gains of business or profession".... -

(ia) any interest commission or brokerage, rent, royalty, fees for professional services or fees for technical services payable to a resident, or amounts payable to a contractor or sub-contractor, being resident for carrying out any work including supply of labour for carrying out any work on which tax is deductible at source under Chapter XVII-B and such tax has not been deducted or, after deduction, has not been paid during the previous year, or in the subsequent year before the expiry of the time prescribed under sub-section (1) of section 200"

From a plain reading of the provision it is clear that the amounts specified under clause (ia) is not allowable as deduction in computing the income chargeable under the head "Profits and gains of business or profession". Similarly, in sub-section (3) of section 40A, it is provided that no deduction shall be allowed in respect of expenditure specified therein. The common feature of both the

provisions is that the expenditure specified in the respective provisions shall not be allowed as a deduction unless the assessee satisfies the condition specified therein. Thus, it can be sent that any expenditure to be allowed as a deduction has to be claimed as such, but in a case where no such claim is made by an assessee, there cannot be any disallowance as held by the coordinate bench in the case of Balaji Engineering and Construction Works (cited supra) which view has also been upheld by the jurisdictional High Court. Therefore, this ground of appeal of the Revenue is rejected."

Under the circumstances the Revenue has preferred the appeals before this court.

5. We may record that as such all matters pertain to the same assessee and for the respective different assessment year but the Commissioner of Income-tax (Appeals) as well as the Tribunal have taken a similar view and the appeals of the Revenue were dismissed. Under the circumstances, the rest of the appeals for the different assessment year are preferred by the Revenue before this court.

6. We have heard Mr. E.I. Sanmathi, learned counsel appearing for the appellants-Revenue and Mr. Chythanya K.K., learned counsel appearing for the respondent-assessee in all the appeals.

7. As such, the matters can be examined in light of question No. 1.

The Tribunal, after appreciation of the evidence has found that the agreement between the assessee and Bapuji was more in the nature of joint venture and was not a subcontract. Such a finding as such in our view is a finding of fact after appreciation and re-appreciation of the evidence initially recorded by the Commissioner (Appeals) and said finding after re-appreciation of the evidence is confirmed by the Tribunal. It is hardly required to be stated that, for the issues based on finding of fact, the Tribunal is the ultimate fact finding authority and this court will not upset the finding of fact unless, such finding of fact is perverse or is contrary to the material on record or based on conjectures and surmises.

8. The learned counsel for the appellant-Revenue has not been able to show any material on the basis of which the finding of fact so concluded by the Tribunal that it was in the nature of joint venture was contrary to the material on record. He only contended that, on appreciation of the evidence, the Tribunal ought not to have concluded that it was in the nature of joint venture and in his submission, the Tribunal ought to have found that it was a sub-contract.

9. In our view, we cannot accept the submission of the learned counsel for the appellant-Revenue for two fold reason ; one is that, there is enough material to show that the amount received of the contract was directly shared by the assessee and Sri Bapuji as per their proportionate share and the second is that: it was not a matter where the money/the amount realized of the contract was apportioned as the income of the assessee and thereafter, the portion of it or a major portion was paid by the assessee to Sri Bapuji. When after receipt of the contract amount, the shares are identified and taken by both the parties of the

joint venture, it cannot be said as a sub-contract. There is no material brought to our notice by the learned counsel for the appellant-Revenue that there was any contract entered into by the assessee to assign the work to Bapuji as sub-contractor. Further, additional aspect is that, when the respective share is received by the assessee, it has been shown as the income by the assessee in the return of income. Same is the situation for the respective share of Sri Bapuji who has shown its income of the amount received by it. Under these circumstances, it is not possible for us to agree with the submission of the learned counsel appearing for the appellant-Revenue that the finding of the Tribunal that it was of joint venture between the assessee and Sri Bapuji was contrary to the material or based on conjectures and surmises.

10. The aforesaid is coupled with the aspects that, upsetting a finding of fact after appreciation and re-appreciation is outside the scope of judicial scrutiny in exercise of appellate power of this court.

11. In view of the above, question No. 1 needs to be answered in negative against the Revenue and in favour of the assessee.

12. On the second question, since provisions of section 40(a)(ia) is already reproduced in the reasons recorded by the Tribunal referred to herein above, we need not reproduce it again. However, if any deduction is claimed from the income as expenses, the question of disallowance of the expenditure or deduction may arise. In the present case, when the assessee has not claimed any amount towards expenditure pertaining to the contract amount which has been received by the assessee, there would not be any scope for disallowing any amount towards the expenditure. The Tribunal has followed the decision of this court in the case of CIT v. Balaji Engineering and Construction Works [2010] 323 ITR 351 (Karn). When the issue is already covered by the decision of this court, it cannot be said that any substantial questions of law would arise for consideration. Hence, question No. 2 need not be answered since the issue is already covered by the above decision in the case of Balaji Engineering Construction Works supra.

13. Apart from the above, there is one additional aspect and the same is that, when the assessee has shown as income of the respective share received by it and when Sri Bapuji has also shown as the income of the amount received by it though may be forming part of common contract and when the income of the respective persons are separately considered and the tax is charged, if additionally the income received by Sri Bapuji is considered for the purpose of taxation in the income of the assessee for the charge-ability of the tax, it would result into double taxation for one income which cannot be maintained nor such is permissible.

14. Hence, question No. 2 shall stand disposed of accordingly as not required to be answered.

15. The other appeals preferred by the Revenue are in respect to the subsequent

assessment years of the very assessee. The Commissioner of Income-tax (Appeals) as well as the Tribunal have adopted the same reasoning as made in the first group of I.T.A.s, i.e., I.T.A. Nos. 103-104/2011.

16. In view of the above referred observation and discussion, we find that the same answer would follow.

17. In the result, question No. 1 is answered in negative against the Revenue and in favour of the assessee. Question No. 2 is not required to be answered.

18. All appeals shall stand disposed of. No order as to cost.