(1991) 03 CAL CK 0020

In the Calcutta High Court

Case No : Income-tax Reference No. 42 of 1987

Commissioner of Income Tax	APPELLANT
Vs	
Gillanders Arbuthnot and Co. Ltd.	RESPONDENT

Date of Decision : 26-03-1991

Acts Referred:
Income Tax Act, 1961 — Section 256

Citation : (1992) 195 ITR 331 : (1993) 69 TAXMAN 31

Hon'ble Judges : Shyamal Kumar Sen, J;Ajit K. Sengupta, J

Bench : Division Bench

Advocate : S.K. Bagchi and R.C. Prasad, for the Appellant;D. Pal and M. Seal, for the Respondent

Judgement

Ajit K. Sengupta, J.—In this reference u/s 256(1) of the Income Tax Act, 1961, the following questions of law have been referred to this court :

"1. Whether, on the facts and in the circumstances of the case, the Tribunal''s finding that the loan of Rs. 48,52,951 was advanced by the assessee-company in the ordinary course of its business is based on relevant and adequate evidence and is reasonable ?

2. On the facts and in the circumstances of the case and especially in view of the fact that part of the loan of Rs. 48,52,951 was advanced by Burlow and Co. Ltd., and not by the assessee-company itself, was the Tribunal justified in holding that the sum of Rs. 21,96,390 out of the aforesaid amount was allowable as a bad debt while computing the assessee''s total income and that it was not a capital loss ?"

2. Shortly stated, the facts are that the assessee is a limited company and derives income from managing agency and from various other sources. Air-conditioning Corporation Limited was a company managed by the assessee-company. Another company, Burlow and Co. Ltd., was a 100% subsidiary company of the assessee-company. The assessee-company became the

managing agent of Air-conditioning Corporation Ltd., on the basis of an agreement dated February 22, 1949, for 20 years. The assessee advanced loan to the said company from lime to time and the loan as on March 31, 1949, stood at Rs. 15,67,147. Thereafter, the said debt was taken over by the 100% subsidiary company of the assessee, viz., Burlow and Co. Ltd. and Burlow and Company Limited, from April 1, 1949, started financing Air-conditioning Corporation Limited on the basis of the agreement dated June 28, 1949. Burlow and Company Limited agreed to finance Rs. 45.1 lakhs to Air-conditioning Corporation Limited. The advance given by Burlow and Company Limited stood at Rs. 49,52,951 as on March 31, 1956. On April 1, 1956, the assessee-company took over the loan granted by its 100% subsidiary Burlow and Company Ltd., and sold the loan to Orient Paper Mills Ltd., a concern belonging to the Birlas in terms of the letter dated April 10, 1956, containing the terms and conditions for a sum of Rs. 26,56,561. The unrealised amount of Rs. 21,96,390 was written off by the assessee-company and the same was claimed as a bad debt and/ or a trading loss.

3. The Tribunal, on these facts, found as follows :

(a) The loan has been granted in the course of the managing agency business of the assessee-company. The Department, at no stage, has doubted the genuineness of the letter dated April 10, 1956, on the basis of which the loan has been purchased by Orient Paper Mills Limited for a lesser amount of Rs. 26,56,561.

(b) Under the circumstances, the transaction was in the course of the business activity of the assessee-company.

(c) As the assessee-company could not realise the loan because the balance of the amount became unrealisable after the debt was purchased by Orient Paper Mills Ltd., it cannot be said that the loan was a capital loss.

(d) The acquisition of the shares and selling out of the loan are two different transactions and they could not be linked together.

(e) The assessee-company was doing the business of financing and, accordingly, it financed Air-conditioning Corporation Limited. Accordingly, the transaction was in the, course of the business activity of the assessee-company and as the assessee company could not realise the loan for the lesser amount which became unrealisable after the debt was purchased by Orient Paper Mills Limited, the same was rightly written off as a bad debt or as a loss.

4. At the hearing, Dr. Pal has submitted that the aforesaid findings and conclusions by the Tribunal are based upon relevant materials and the Revenue has not pointed out what irrelevant materials have been relied on by the Tribunal in arriving at its findings.

5. On the other hand, the contention of the Revenue is that the loan was advanced by Burlow and Co. Ltd., and not by the assessee and, accordingly, no

deduction can be allowed to the assessee in respect of the loan stated to have become bad or irrecoverable.

6. We have considered the rival contentions, Burlow and Company was a 100% subsidiary of Gillanders Arbuthnot and Co., Ltd. In the agreement itself which was entered into on June 28, 1949, it was stated that, at the request of Burlow and Co., Gillanders Arbuthnot (being the lender in the said agreement) has agreed to grant financial accommodation to Burlow and Company by way of loan or overdraft on cash credit account up to a limit of Rs. 45 lakhs. It was further agreed that all book debts and outstandings due or to become due to Burlow and Company in respect of the business including the right, title and interest of Burlow and Company under hypothecation created by, inter alia, Air-conditioning Corporation Limited in favour of the company and all benefits arising thereunder would be hypothecated to Gillanders Arbuthnot.

7. The said agreement dated June 28, 1949, by or between Burlow and Company Limited (referred to as company) and the assessee (referred to as the lender) provides that, at the request of the company, the lender has agreed to grant financial accommodation to the company by way of loan or overdraft or cash credit account up to and not exceeding in the aggregate, at any one time, the maximum limit of rupees forty-five lakhs payable with interest thereon at the rate hereinafter mentioned on the security hereof. Clause 1 of the said agreement provided as follows :

1. In pursuance of the said agreement and in consideration of the premises, the company doth hereby hypothecate to the lender first the goodwill of the business and trade carried on by the company, secondly, all book debts and outstandings due or to become due to the company in respect of the said business expressly including the right, title and interest of the company under hypothecations created by Mackintosh Burn Ltd., Air-conditioning Corporation Ltd., D. Waldie and Co. (Lead Oxides) Ltd., Waldies Industries Ltd., and the Bangalore White lead Syndicated Ltd., in favour of the company and all benefits arising thereunder, thirdly, the benefits of all pending contracts and all other property and assets of the company used in connection with the said business (hereinafter collectively referred to as "the said assets and property") by way of first charge as continuing security for the payment to the lender, on demand, of the balance for the time being due and owing by the company to the lender on the said overdraft or cash credit account (hereinafter called "the said account") and for the payment and discharge of all present and future indebtedness and liabilities of the company to the lender of any kind in any manner whether solely or jointly primarily or collaterally accrued or contingent with all relative interest charges costs (as between attorney and client) and expenses together with interest thereon in the said account to be kept and made up with interest on the daily debit balance at such rate of interest and with such rests in account as may be agreed between the lender and the company until payment and costs as hereinafter mentioned.

8. It will, therefore, appear that the Burlow and Company will be financing Air-conditioning Corporation and, for such financing, Gillanders Arbuthnot will be granting financial accommodation to Burlow and Company up to Rs. 45 lakhs. The book debts and also the right, title and interest of the company under hypothecation created by Air-conditioning Corporation will be hypothecated to Gillanders Arbuthnot. In other words, Gillanders Arbuthnot will be entitled to the benefit of hypothecation of the book debts made by Air-conditioning Corporation in favour of Burlow and Co. The resolution of the company dated June 8, 1949, makes it clear that, in view of the fact that Gillanders Arbuthnot is prohibited from financing, inter alia, Air-conditioning Corporation, Burlow and Co. is to give such companies the required finance and, therefore, Burlow and Co., will be given advance by Gillanders Arbuthnot to the extent of Rs. 45 lakhs. Financing is one of the objects in the memorandum of both Gillanders Arbuthnot and Burlow and Company.

9. The memorandum of association empowered the assessee to raise finance. Clauses 8 and 9 of the memorandum of association are as follows :

"8. To carry on the business of banking in all its branches and departments, including the borrowing, raising or taking up of money, the lending or advancing of money on securities and property, the discounting, buying, selling and dealing in of bills of exchange, promissory notes, coupons, drafts, bills of lading, warrants, debentures, certificates, scrips and other instruments and securities, whether transferable or negotiable or not, the granting and issuing of letters of credit and circular notes, the buying, selling and dealing in bullion and specie, the acquiring, holding, issuing on commission underwriting and dealing with stocks, funds shares, debentures, debenture-stocks, bonds, obligations and other investments and securities and investments of all kinds, the negotiating of loans and advances, the receiving of money and valuables on deposit or for safe custody or otherwise, the collecting and transmitting of money and securities, the managing of property and transacting all kinds of agency business commonly transacted by bankers.

9. To advance or lend any of the moneys of the company whether being capital or loan moneys or otherwise for the time being on the security of lands of any tenure incorporeal rights, rates or bills duly authorised to be made or levied by any Government or local municipal authority or the republic body, bills of exchange, promissory notes, bonds, commercial documents, policies of assurance, produce, stock-in-trade, chattels, securities and other property both immovable or movable of whatsoever nature or kind and whether situate in British India or elsewhere and in such form and on such terms as the company shall think fit or if the company shall think fit without security and generally to lend money to such persons or companies whether with or without security and on such terms as may seem expedient and in particular to customers and others having dealings with the company."

10. Clauses 3(g) and 3(h) of the memorandum of association of Burlow and

Company have provided for the following objects :

"g. To carry on business as capitalists and financiers, and to undertake and carry on, and execute, all kinds of financial, commercial, trading and other operations, except the issuing of policies of assurance on human life ; to advance or lend money to such persons and on such terms as may seem expedient, to discount, buy, sell and deal in bills, notes, warrants, coupons and other negotiable or transferable securities or documents.

h. To lend money to and guarantee the performance of the obligations of and the payment of the capital and principal of and dividends and interest on any stock, shares and securities of any company, firm or person in any case in which such loan or guarantee may be considered likely directly or indirectly to further the objects of this company or the interest of its members and in particular to guarantee the overdraft or cash credit account of any person or persons, company or companies with any financier or bank including the Imperial Bank of India."

11. The accounts position of Burlow and Company also makes it clear that before June, 1949, the audited accounts do not show any amount of advance received from Gillanders Arbutlmot or that any loan was advanced to the companies referred to in the agreement. After 1949, the accounts will show that Gillanders Arbuthnot has advanced sums to the extent of Rs. 11,97,774 on current account for the year ending March 31, 1950, and correspondingly also, advances were made to the different companies to the extent of Rs. 18,26,021. The position up to 1956 will appear in the balance-sheet for the year ending March 31, 1956. The secured loan from Gillanders Arbuthnot is Rs. 45 lakhs and the unsecured loan from Gillanders Arbuthnot is Rs. 10,16,512. Against that, the advance made by Burlow and Co. to the different companies referred to in the agreement is Rs. 58,43,089. In the balance-sheet for the year ending March 31, 1957, when the entire loan was taken over by Gillanders Arbuthnot, the advance also shown to have been made to the different subsidiary companies did not appear in the balance-sheet of Burlow and Co. for the year ending March 31, 1956.

12. From the aforesaid position, it will be clear that because of certain difficulties, Gillanders Arbuthnot could not directly advance the loan to its managed companies like Air-conditioning Corporation. It was really to the 100% subsidiary, Burlow and Co., that advances were made and all the book debts which were hypothecated by Air-conditioning Corporation and other subsidiary companies were hypothecated to Gillanders Arbuthnot. Therefore, Burlow and Co. was really a medium or a conduit pipe through which finances were made by Gillanders Arbuthnot and when, in 1957, the entire loan advanced by Burlow and Co. was taken over, the balance-sheet of Burlow and Co. also wipes off the advances given by Gillanders Arbuthnot and also the loan given to the different subsidiary companies by Burlow and Co. Thus, the finance was really made by Gillanders Arbuthnot and such financing to the managed company was incidental to the business of managing agency. Hence, when the entire book debts

amounting to Rs. 48,52,951 as on March 31, 1956, were assigned and taken over by Orient Paper Mill for a sum of Rs. 26,56,561, the unrealised amount of Rs. 21,96,390 was written off by the assessee-company as a bad debt and/or a trading loss. When the debt was written off, the directors'' report for the year ending March 31, 1957, also may be looked into.

13. We may add in this connection that the case of the assessee came up for hearing before this court-see Commissioner of Income Tax Vs. Gillanders Arbuthnot and Co. Ltd., . There, a Division Bench of this court held that the assessee was engaged in the business of financing its subsidiaries or that, at any rate, financing the subsidiaries was incidental to the assessee''s main business activities which were diverse in nature.

14. For the foregoing reasons, it must be held that the loss incurred by the assessee in financing its subsidiary must be allowed as a business loss.

15. We, therefore, answer both the questions in this reference in the affirmative and in favour of the assessee.

16. There will be no order as to costs.

Shyamal Kumar Sen, J.

17. I agree.