(2005) 03 GUJ CK 0015

In the Gujarat High Court

Case No : IT Ref. No. 87 of 1993

Commissioner of Income Tax — APPELLANT

Vs

Gujarat Carbon Ltd. — RESPONDENT

Date of Decision : 14-03-2005

Acts Referred:
Income Tax Act, 1961 — Section 256(1), 37(1), 37(2), 37(2A)

Citation : (2005) 196 CTR 614 : (2005) 277 ITR 349

Hon'ble Judges : H.N. Devani, J;D.A. Mehta, J

Bench : Division Bench

Advocate : Manish R. Bhatt, for the Appellant; Manish J. Shah, for J.P. Shah, for the Respondent

Judgement

D.A. Mehta, J.—The Tribunal, Ahmedabad Bench ''A'', has referred the following question for the opinion of this Court u/s 256(1) of the IT Act, 1961 (the Act), at the instance of the CIT, Ahmedabad :

"Whether the Tribunal is right in law and on facts in deleting the additions made by the ITO amounting to Rs. 16,121 on account of presentation articles as also an amount of Rs. 35,226 as sales expenses which according to the ITO were hit by the provisions of Section 37(2A) ?"

2. The assessment year is 1984-85 and the relevant accounting period is previous year ended on 30th June, 1983. The assessee, a public limited company filed return on 31st July, 1984, disclosing total income of Rs. 20,55,630. The assessment was framed on 27th Feb., 1987, on total income of Rs. 41,16,769. During the course of assessment, the AO disallowed the sums of Rs. 16,121 on account of presentation articles and Rs. 35,226 shown as sales expenses. It appears that the latter sum of Rs. 35,226 included expenses incurred on cigarettes for guests of the company, purchase of handicraft articles and tea packets, etc. According to the AO both the items of expenditure were incurred for entertaining the guests of the company and hence, the expenditure fell within the ambit of provisions of Section 37(2A) of the Act read with Expln. 2 to the

said section. The assessee carried the matter in appeal before the CIT(A) who for the reasons stated in his order dt. 23rd Feb., 1988, confirmed the disallowance. The assessee carried the matter in second appeal before the Tribunal who for the reasons stated in its order dt. 29th Aug., 1992, allowed the appeal by holding as follows :

"On carefully going through the records and hearing both the parties, we are of the opinion that these expenditure are incurred in the course of business for the best interest of business and expended wholly and exclusively for the purpose of business. As we noted earlier, all entertainment may imply hospitality but all hospitality under all circumstances cannot be considered as entertainment. Taking into consideration the total turnover, the expenditure claimed by the assessee is negligible. This ground is decided in favour of assessee".

3. Heard Mrs. M.M. Bhatt, learned standing counsel on behalf of the applicant-Revenue. She has placed reliance on case of Commissioner of Income Tax Vs. Arvind Mills Ltd., She submitted that none of the items of expenditure had been incurred for employees of the assessee-company and in these circumstances in light of Expln. 2 to Section 37(2A) of the Act, the amounts had rightly been disallowed by the AO; that the Tribunal was in error in allowing the same.

4. As against that Mr. Manish J. Shah, learned advocate appearing on behalf of the respondent-assessee, submitted that insofar as the item of expenditure of Rs. 16,121 was concerned, the same had been incurred on account of presentation articles and in no view of the matter could the same be considered as entertainment expenditure. That such expenditure was incurred for the purpose of developing and maintaining the goodwill of the assessee-company and was not incurred for providing any entertainment. That even if Expln. 2 to Section 37(2A) of the Act was taken into consideration, the nature of expenditure of Rs. 16,121 had to be borne in mind and the expenditure incurred for presentation articles could not be brought within the sweep of the provision howsoever wide the term ''entertainment expenditure'' is construed. In support, reliance is placed on the following decisions of this Court :

(1) Commissioner of Income Tax, Gujarat-I Vs. S.L.M. Maneklal Industries Ltd.,

(2) COMMISSIONER OF Income Tax, GUJARAT-III Vs. DASCROI TALUKA CO-OPERATIVE PURCHASE AND SALES UNION LTD.,

(3) Karjan Co-operative Cotton Sales Ginning and Pressing Society Vs. Commissioner of Income Tax,

5. Section 37(2A) of the Act opens with non obstante clause whereby it is laid down that no allowance shall be made in respect of so much of the expenditure in the nature of entertainment expenditure incurred by any assessee during any previous year which expires after the 30th day of September, 1967, except to the extent of specified limit laid down in the section. Therefore, any expenditure which is otherwise allowable u/s 37(1) or 37(2) of the Act, would be hit by

provisions of Section 37(2A) of the Act if the expenditure is in the nature of entertainment expenditure. Expln. 2 to the said section was inserted by Finance Act, 1983, with retrospective effect from 1st April, 1976, and it gives an inclusive definition of the term "entertainment expenditure" so as to include 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. The rest of the portion of the Explanation is not relevant for the present. In these circumstances, the question which falls for consideration is whether expenditure incurred on presentation articles can be termed to be either entertainment or providing of hospitality, whether by way of food or beverages or in any other manner whatsoever.

6. In the case of CIT v. Patel Brothers & Co. Ltd. and Ors. : [1995]215ITR165(SC) , the apex Court as called upon to decide this very controversy. The Supreme Court after taking into consideration : (i) the provision as it stood before insertion of Expln. 2 to Section 37(2A)w of the Act, (ii) as well as the position after insertion of the Explanation, and (iii) contemporaneous circular issued by the Board and the scheme of the Act held that :

"Generally, ''entertainment expenditure'' is an expression of wide import. However, in the context of disallowance of ''entertainment expenditure'' as a business expenditure by virtue of Sub-section (2A) of Section 37, the word ''entertainment'' must be construed strictly and not expansively. Ordinarily, ''entertainment'' connotes something which may be beneficial for mental or physical well being but is not essential or indispensable for human existence. A bare necessity, like an ordinary meal, is essential or indispensable and, therefore, is not ''entertainment''. If such a bare necessity is offered by another, it is hospitality but not entertainment. Unless the definition of ''entertainment'' includes hospitality, the ordinary meaning of ''entertainment'' cannot include hospitality. For this reason, the expenditure incurred in extending customary hospitality by offering ordinary meal as a bare necessity, is not ''entertainment expenditure'' without the aid of the enlarged meaning given to the words by Expln. 2 inserted w.e.f. 1st April, 1976. The definition in Expln. 2 is not the ordinary meaning of the words ''entertainment expenditure'' but the enlarged meaning given for the purpose of the Act w.e.f. 1st April, 1976"

7. Thus, it becomes clear that the term ''hospitality'' normally cannot be included in the ordinary meaning of the term ''entertainment'', but falls within the enlarged meaning given to the words by Expln. 2 to Section 37(2A) of the Act. It is apparent that the expenditure in question cannot be termed to be entertainment ordinarily, because it connotes something which is beneficial for mental or physical well being but is not essential or indispensable for human existence. Hence, normal meaning of term ''hospitality'' is required to be taken into consideration in absence of any definition under the Act. The said term as defined in the dictionary "Oxford Advanced Learner''s Dictionary (2000 Edn.)" reads as under :

"hospitality 1 friendly and generous behaviour towards guests : Thank you for your kind hospitality. 2 food, drink or services that are provided by an organisation for guests, customers, etc. : We were entertained in the company''s hospitality suite--the hospitality industry (= hotels, restaurants, etc.)"

8. Applying the aforesaid test enunciated by the apex Court, it cannot be stated that the expenditure in question viz., Rs. 16,121 incurred towards presentation articles would fall either within the meaning of the term ''entertainment'' or ''hospitality''. If that be so, the expenditure in question cannot be termed to be either entertainment expenditure or in the nature of entertainment expenditure. Therefore, the conclusion of the Tribunal that the said item of expenditure viz., Rs. 16,121 cannot be termed to be entertainment expenditure is correct though for the reasons stated hereinbefore.

9. The other sum of Rs. 35,226 described as sales expenditure is on the application of the above tests an item of expenditure which would fall within the meaning of the term entertainment expenditure, as the said expenditure had been incurred for extending hospitality to various persons as detailed in the assessment order viz., guests of the company. The Tribunal was, therefore, not correct in holding that the sum of Rs. 35,226 shown as sales expenditure by respondent-assessee was not entertainment expenditure so as to be hit by provisions of Section 37(2A) read with Expln. 2 to the said section.

10. In the result, the question referred to the Court is answered partly in affirmative and partly in negative i.e., the Tribunal was right in law in deleting the addition by way of disallowance of Rs. 16,121 on account of presentation articles, but the Tribunal was not correct in deleting the addition by way of disallowance amounting to Rs. 35,226 on account of sales expenses. Reference is accordingly answered, partly in favour of the respondent-assessee and partly in favour of the applicant-Revenue as stated hereinbefore and stands disposed of accordingly. There shall be no order as to costs.