(1990) 02 KL CK 0043

In the High Court Of Kerala

Case No : Income-tax Reference No. 51 of 1986

Commissioner of Income Tax APPELLANT

Vs

Kilco Refrigeration RESPONDENT

Date of Decision : 06-02-1990

Acts Referred:
Income Tax Act, 1961 — Section 255, 256

Citation : (1990) 183 ITR 318

Hon'ble Judges : Varghese Kalliath, J;K.S. Paripoornan, J

Bench : Division Bench

Advocate : P.K. Ravindranatha Menon and N.R.K. Nair, for the Appellant; P.C. Chacko, for the Respondent

Judgement

Varghese Kalliath, J.—At the instance of the Commissioner of Income Tax, Cochin, the Income Tax Appellate Tribunal (for short, "the Tribunal"), Cochin Bench, has referred the following questions of law for the opinion of this court.

"(1) Whether, on the facts and in the circumstances of the case, the Tribunal was justified in interfering with the disallowance of Rs. 74,000 ordered by the Income Tax Officer and confirmed by the Commissioner of Income Tax (Appeals) ?

(2) Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that Rs. 74,000 should be treated as outgoings for the purpose of the business of the assessee ?

(3) Whether, on the facts and in the circumstances of the case, the Tribunal did have materials to hold that ''the assessee has not retained any part of this sum of Rs. 74,000 in its hands'' or ''it has received the amount one particular day and has also returned it on the same day to Messrs. Paksons Industries through the medium of these ten persons'' ?

(4) Was the doctrine of real income, adopted by the Tribunal, applicable to the facts and circumstances of the case ?"

2. These questions were referred by the Tribunal as directed by the judgment of this court in O. P. No. 3271 of 1974. The assessee is a registered firm. The assessment year in question is 1978-79 for which the previous year ended on December 31, 1977. The assessee had business dealings as agents and stockists of its principals. The assessee executed certain contracts for a firm by name Messrs. Paksons Industries. The total amount of the contract was Rs. 3,54,000. Messrs. Paksons Industries had obtained financial assistance from the Kerala Financial Corporation.

3. On December 29, 1977, it is seen that the assessee had received a sum of Rs. 74,000 in the form of a demand draft from Messrs. Paksons Industries. It is also seen that, on the same day, the assessee had purported to have paid Rs. 74,000 to ten different persons. The finding of the Income Tax Officer is that the said amount of Rs. 74,000 had ultimately reached Messrs. Paksons Industries. Before the Income Tax Officer, it was claimed by the assessee that the amount of Rs. 74,000 was paid as commission to ten persons. The Income Tax Officer found that since the assessee failed to establish the payments as stated by him and since there was no question of any commission payment, the amount cannot be allowed as a deduction.

4. The assessee filed an appeal before the Commissioner of Income Tax (Appeals). The Commissioner of Income Tax (Appeals) agreed with the Income Tax Officer. He held that the sum of Rs. 74,000 claimed to have been paid as commission to the ten persons was not in reality a commission payment, that it was a payment to the nominee of Messrs. Paksons Industries in order to help the latter to literally repay the loan taken from the Kerala Financial Corporation. It was further found that the payment cannot be classified as an expenditure incurred for the purpose of the business of the assessee. In his opinion, the contention of the assessee that, if the assessee had not agreed to this arrangement, it would not have got the contract, could not be accepted as a nexus between the business of the assessee and the payment of the commission.

5. The assessee filed an appeal before the Tribunal. The Tribunal found that the amount of Rs. 74,000 could not be treated as the income of the assessee. The Tribunal proceeded on the basis of the finding of fact that Rs. 74,000 had left the coffers of the assessee and that no specific service was rendered to the assessee by the ten persons in return for the payments. But, the Tribunal accepted the explanation of the assessee that, by this amount, the contract amount has been correspondingly increased and there was no net gain to the assessee from this particular transaction. The effect of these findings is that Rs. 74,000 was received from Messrs. Pak-sons Industries and it was returned to Messrs. Paksons Industries through "the dubious methods" adopted by the assessee. The Tribunal also found that there has been "an active collusion" between the assessee and Messrs. Paksons Industries for putting up artificially the cost of a freezing plant, which the assessee had contracted to do for them and that the purpose of this was only to enable Messrs. Paksons Industries to get a higher

amount as loan from the Kerala Financial Corporation. The final finding of the Tribunal was that the assessee had not retained any part of this sum of Rs. 74,000 in its hands and that it had received the amount on a particular day and returned the same on that day itself to Messrs. Paksons Industries through the medium of ten persons and so the sum of Rs. 74,000 could not be said to be the "real income" of the assessee. In the result, the Tribunal deleted the disallowance of Rs. 74,000. To support this conclusion, the Tribunal has relied on the decision of the Madras High Court in Commissioner of Income Tax, Madras Vs. Coimbatore Salem Transport (Private) Limited., . The Revenue was aggrieved and at the instance of the Revenue, the questions set out in paragraph 1 of this judgment have been referred to this court for its decision.

6. We heard counsel on both sides. In the order of the Tribunal, it is seen stated that one of the persons who ostensibly received the commission was a partner of Messrs. Paksons Industries. The Tribunal understood the contention of the assessee as an arrangement to receive an amount of Rs. 74,000 from Messrs. Paksons Industries only to be returned to Paksons Industries in the method stated by the assessee in order to help Messrs. Paksons Industries "to obtain a higher amount as loan from the Kerala Financial Corporation". Of course, the assessee has stated that the amount has been paid as commission to ten persons and that the assessee has not received any service for the said payment. The Tribunal has further said that the Commissioner of Income Tax (Appeals) has found, on the facts disclosed, that the net result of the arrangement was that the sum of Rs. 74,000 claimed to have been paid as commission to the ten persons was not in reality a commission payment and that it was a payment to the nominee of Messrs. Paksons Industries. The Tribunal also referred in its order to the opinion of the Commissioner of Income Tax (Appeals) that the claim of repayment had nothing to do with the business carried on by the assessee and that the payment has not been made by the assessee in their capacity as traders and "that it has been paid by the assessee as abettors in a scheme to draw out more money from the Kerala Financial Corporation" than the rules would permit, and that this was not part of the assessee''s business. The assessee''s case is that if the assessee had not agreed to the above arrangement, the assessee would hot have got the contract.

7. The rival contentions of the assessee and the Department were considered by the Tribunal. The Tribunal found that the sum of Rs. 74,000 cannot be treated as the income of the assessee. It also referred to the claim of the assessee that it was an expenditure laid out wholly and exclusively for the purpose of its business. It is pertinent to note that the Tribunal has observed thus :

"Though the Income Tax Officer had taken great pains to establish the sham nature and the devious method employed by the assessee in collaboration with Messrs. Paksons Industries to make out that a sum of Rs. 74,000 has been paid as commission in return for services rendered by the ten persons, the assessee does not stick to this position as is evident from the submissions made by it before the Commissioner of Income Tax (Appeals). We may, therefore, proceed on the basis that though the sum of Rs. 74,000 has, in fact, left the coffers of the assessee, no specific services were obtained by the assessee from the ten persons in return for this payment."

8. The Tribunal found that it has been fairly well established by the assessee that, but for this agreed arrangement, it could not have been able to secure the contract. The Tribunal has stated that the Income Tax Officer himself has traced the ten recipients to whom the amount has been paid, and that "there has been an active collusion" between the assessee and Messrs. Paksons Industries for putting up "artificially" the cost of the freezing plant and that this conduct would clearly show that the assessee had not retained any part of the sum of Rs. 74,000 in its hands. Finally, the Tribunal, relying on Commissioner of Income Tax, Madras Vs. Coimbatore Salem Transport (Private) Limited., , held that "if, in the instant case, the sum of Rs. 74,000 is considered to be part of the receipt of the assessee under the contract, then the expenditure of Rs. 74,000 should also be considered as an expenditure incurred in the course of the business of the assessee." Holding so, the Tribunal upheld the claim of the assessee for the deduction of the amount from the business income of the assessee.

9. Counsel for the assessee referred us to the decision in Commissioner of Income Tax Vs. Karam Chand Thapar and Bros. P. Ltd., , where Kama J. has observed that "the Tribunal is the final fact-finding body. The questions whether a particular loss is a trading loss or a capital loss and whether the loss is genuine or bogus are primarily questions which have to be determined on an appreciation of the facts. The findings of the Tribunal on these questions are not liable to be interfered with unless the Tribunal has taken into consideration any irrelevant material or has failed to take into consideration any relevant material or the conclusion arrived at by the Tribunal is perverse in the sense that no reasonable person, on the basis of facts before the Tribunal, could have come to the conclusion to which the Tribunal has come." Counsel also relied on the observation of Kania J. in the same judgment that this court should not consider that it is its obligation in a reference case to scrutinise the decision of the Tribunal sentence by sentence to find out whether all facts have been set out in detail by the Tribunal or whether some incidental fact which appears on the record has not been noticed by the Tribunal in its judgment. The obligation of this court is to decide the question of law referred to it on a fair reading of the judgment of the Tribunal and to see whether the Tribunal has taken into account all relevant material and has not taken into account any irrelevant material in basing its conclusions. If the Tribunal has not erred in this area, the decision of the Tribunal is not liable to be interfered with, unless the conclusions arrived at by the Tribunal are perverse. In short, counsel submitted that the decision of the Tribunal is essentially based on appreciation of facts and this court should not interfere with the findings recorded by the Tribunal.

10. Counsel for the assessee submitted that even if the assessee agreed to

execute the contract with Messrs. Paksons Industries for an inflated amount so as to enable Messrs. Paksons Industries to obtain a larger amount from their financing agency, the amount of Rs. 74,000 paid by the assessee through the ten persons which ultimately reached Messrs. Paksons Industries cannot be taken as the business income of the assessee. Counsel referred us to the decision in Commissioner of Income Tax, Patiala Vs. Piara Singh, , wherein the Supreme Court had occasion to consider the case of an assessee, who while carrying on smuggling activity, was apprehended by the Indian police, while crossing the border into Pakistan, and a sum of Rs. 65,000 in currency notes was recovered from his person. On interrogation, the assessee stated that he was taking the currency notes to Pakistan to purchase gold there and smuggle it into India. The customs authorities confiscated the currency notes. The Income Tax authorities found that the assessee was carrying on the business of smuggling and that he was liable to pay Income Tax on income from that business and such income was assessed to tax. The question was whether the assessee was entitled to deduction of the loss of Rs. 65,000 arising by the confiscation of the currency notes. The Supreme Court held that "the carriage of the currency notes across the border was an essential part of the smuggling operation and detection by the customs authorities and the consequent confiscation was a necessary incident and constituted a normal feature of such an operation". It was found that "the confiscation of the currency notes was a loss occasioned in pursuing the business of smuggling. It was a loss in much the same way as if the currency notes -had been stolen or dropped on the way while carrying on the business. It was a loss which sprang directly from the carrying on of the business and was incidental to it and its deduction had to be allowed u/s 10.".

11. Counsel referred us to Usher''s Wiltshire Brewery Ltd. v. Bruce [1915] AC 433, where Lord Sumner observed thus (at page 469) :

"Where the whole and exclusive purpose of the expenditure is the purpose of the expender''s trade, and the object which the expenditure serves is the same, the mere fact that to some extent the expenditure enures to a third party''s benefit, say that of the publican, or that the brewer incidentally obtains some advantage, say in his character of landlord, cannot in law defeat the effect of the finding as to the whole and exclusive purpose."

12. In British Insulated and Helsby Cables Ltd. v. Atherton [1926] AC 205 ; [1925] 10 TC 155, Lord Cave observed thus (at page 191 of 10 TC):

"It was made clear in the above cited cases of Usher''s Wiltshire Brewery v. Bruce [1915] AC 433 and Smith (J. W.) v. Incorporated Council of Law Reporting for England and. Wales [1914] 3 KB 674, that a sum of money expended, not of necessity and with a view to a direct and immediate benefit to the trade, but voluntarily and on the grounds of commercial expediency, and in order indirectly to facilitate the carrying on of the business, may yet be expended wholly and exclusively for the purposes of the trade."

13. Rowlatt J. in Mitchell v. B.W. Noble Ltd. [1927] 1 K. B. 719 held that "the money spent on getting rid of a director and saving the company from scandal was deductible". This decision was affirmed by the Court of Appeal and the Court of Appeal held that "as the payment was not made to secure an actual asset so as effectually to increase the capital of the company but was made in order to enable the directors to carry on the business of the company as they had done in the past unfettered by the presence of the retiring director, which might have had a bad effect on the credit of the company, it must be treated as revenue and not as capital expenditure and was deductible as such for Income Tax purposes".

14. The reasoning and conclusion of the Appellate Tribunal dealing with the rival pleas put forward by the parties is contained in paragraphs 4 and 5 of its appellate order dated February 28, 1983. The said order, read as a whole, is vague and contains generalisations, which border on inconsistencies and contradictions, rendering the conclusion as one based on shaky and fragile foundations. The duty of the Appellate Tribunal is to render positive and precise findings on facts and then state its conclusions. It has failed to do so. The order of the Appellate Tribunal is vitiated. The Appellate Tribunal states that the particular arrangement between the assessee and Messrs. Paksons is a "collusive arrangement between the parties, that the Commissioner of Income Tax has opined that there was ''active collusion'' and that the arrangement might have shades of illegality", and "that the make believe arrangement between the parties was not in order to minimise the tax liability of the assessee, etc." If the arrangement was "collusive", meaning that it is fraudulent, a party to the arrangement cannot take advantage of it. That principle has not been applied herein, Why ? If the arrangement was only "make believe" (sham), nothing took effect. In reality, there "was no payment as also no receipt". The entire thing should have been ignored, as a package. Why was it not so done ? What the Appellate Tribunal meant in the passages stated above is neither clear nor intelligible. Then again, the Tribunal proceeded on the basis that the sum of Rs. 74,000 left the coffers of the assessee, that the 10 persons to whom it was alleged to have been made payments, rendered no specific services, that the recipients were henchmen of Messrs. Paksons, and that the assessee has not retained any part of this sum in its hands, what it received on a particular day has been returned on the same day, and so it cannot be said that the said sum of Rs. 74,000 was in reality received by the assessee and so was not its "real income". But, the Tribunal concluded by stating that, if the sum is considered to be part of the receipt, then the expenditure was incurred in the course of the business of the assessee and so the claim for deduction is to be upheld. The above vague generalisations show that the Tribunal was not sure whether the receipts and payments took effect at all and the legal effect of the transactions as a whole in that perspective and even if the apparent transactions were to be given effect to, what is the legal import in the instant case ? These and other aspects deserve examination. We are not to be understood as upholding or approving either the approach or the vague generalisations stated above in any

manner.

15. In the result, we are of the view that the crucial findings of the Tribunal are not clear and they border on inconsistencies and so we decline to answer the questions referred to us. However, we direct the Appellate Tribunal to decide the matter afresh in the light of the various aspects highlighted by us in this judgment.

16. The reference is answered as above.

17. A copy of this judgment under the seal of this court and the signature of the Registrar shall be forwarded to the Income Tax Appellate Tribunal, Cochin Bench, forthwith.

